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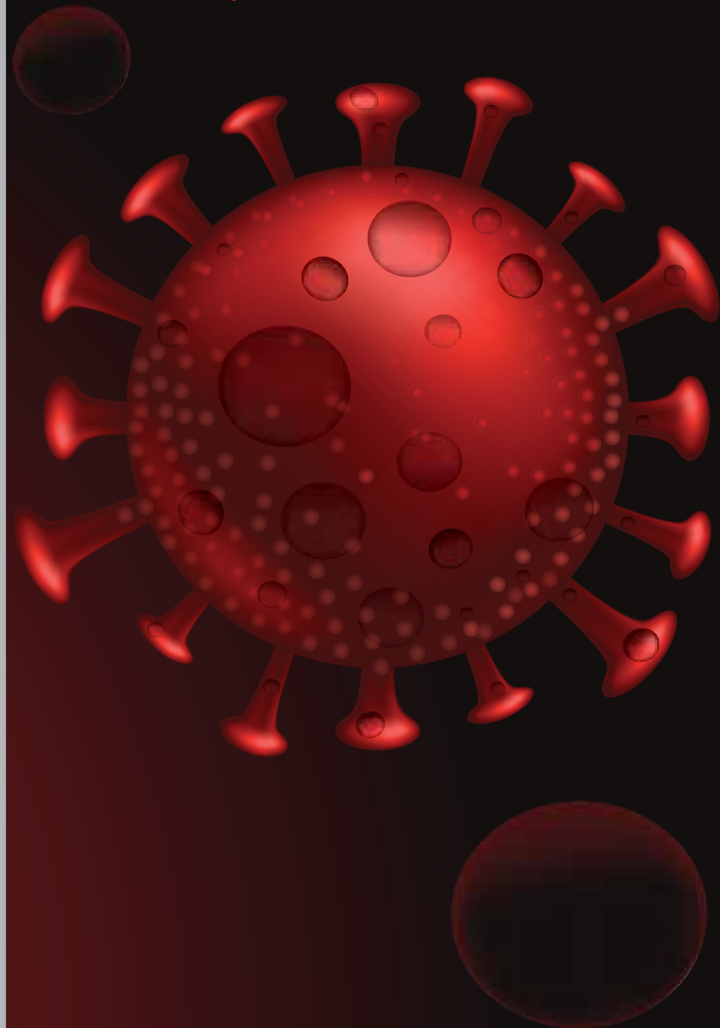
TRADE AND DEVELOPMENT REPORT UPDATE

The Covid-19 Shock to Developing Countries:

Towards a "whatever it takes" programme for the two-thirds of the world's population being left behind

MARCH 2020



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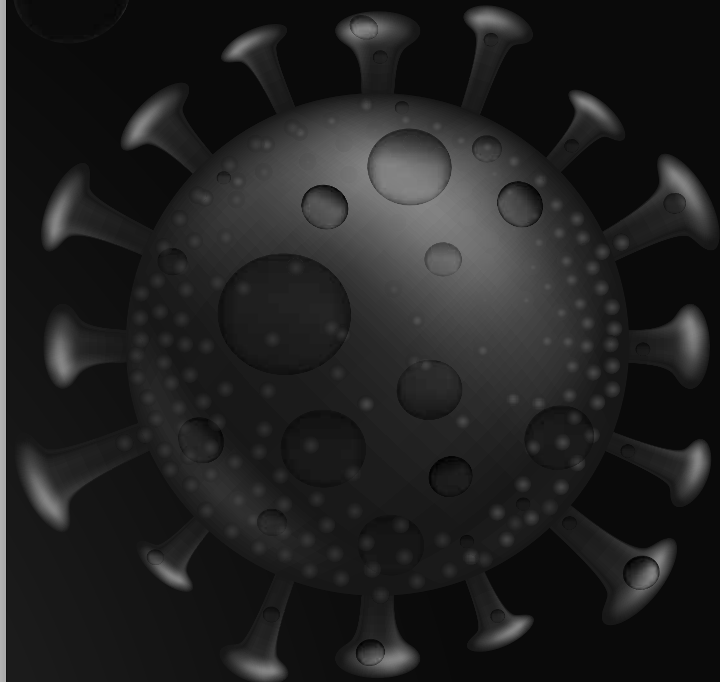

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Averting global depression

Projections of the potential impact of the Covid-19 shock on economies around the world for the year 2020 vary widely. However, there is broad agreement that the global economy will contract given the sudden stop to large swathes of activity and the resulting income loss in the manufacturing and services sectors across most advanced countries and China, combined with the adverse effects on financial markets, consumption (through both income and wealth effects), investment confidence, international trade and commodity prices.

For advanced country governments, now scrambling to contain the economic impact of the Covid -19 pandemic, the challenge -- as discussed in our first *Trade and Development Report Update*[1] -- is compounded by persistent fragilities surrounding highly speculative financial positions, in particular, the already unsustainable debt burdens associated with highly leveraged corporate loans. These have been built up over the last decade of easy money and against a backdrop of heavily underregulated 'high-tech-cum-gig economies' and deeply ingrained income inequalities. In addition, the avalanche of cheap credit since 2008 has also spilled over to developing countries, creating new financial vulnerabilities and undermining their debt sustainability.

In the past days a series of stimulus packages -- unprecedented in both scale and scope -- have been announced by the major developed economies and China to extenuate the mounting economic damage and respond to the health crisis. Aside from financial injections to keep the banking and corporate balance sheets on relatively stable footing, the critical measures to avert contractions of economic activity include government spending (particularly on health care), extended unemployment benefits and cash transfers.

The details still need to be carefully examined but some broad estimates can be made about how this will likely translate into additional demand and thus national income in each economy. Employing our Global Policy Model, we estimate a boost to the national incomes of advanced economies and China of about $1.4 trillion in 2020, substantially smaller than the headline values of the packages.[2] This no doubt will have a positive impact not only on their own economies but the world economy as well.

Although this will, in all likelihood, not prevent a global contraction this year it should (hopefully) avert the recession turning in to a prolonged depression. It should also contribute to stemming the fall in the prices of both financial assets and commodities and will partially alleviate the negative growth impact from the crisis on developing countries.

Developing countries, however, face distinct pressures and constraints which make it significantly harder for them to enact effective stimulus without facing binding foreign exchange constraints. And as these countries do not issue international reserve currencies, they can only obtain them through exports or sales of their reserves. What is more, exports themselves require significant imports of equipment, intermediate goods, know-how and financial business services. Finally, the financial turmoil from this crisis has already triggered sharp currency devaluations in developing countries, which makes servicing their debts and paying for necessary imports for their industrial activity far more onerous.

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[1] https://unctad.org/en/PublicationsLibrary/gds_tdr2019_update_coronavirus.pdf

[2] The "stimulus packages" adopted in developed economies and China contain both emergency measures, such as loans to keep businesses solvent while economies are shut down, and demand injections, such as government purchases of goods and services and money transfers to households. The latter are a fraction of the packages adopted. For example, in the US$2.2tn package adopted by the United States these measures amount to less than US$579bn, including spending in goods and services ($193bn), additional unemployment benefits (an estimated $111bn) and cash transfers ($275bn). The largest share of the package comprises loans to business, which may turn in to transfers if they are not repaid. Barring this event and considering the multiplicative effect of government spending on GDP and the fact that cash benefits are partially saved, the additional demand in 2020 generated by these measures is an estimated US$395bn, less than one-fifth of the package's face value.

The shock of the lightning

Many developing countries were slowing down in the final quarter of last year with several entering recession. However, the speed at which the economic shock to advanced economies has hit developing countries – in many cases in advance of the health pandemic -- is dramatic, even in comparison to the 2008 global financial crisis.

As Figure 1.a below shows, net portfolio flows, both debt and equity, from main emerging economies amounted to $59 billion in the month since the Covid-19 crisis went global (21 February to 24 March). This is more than double the portfolio outflows experienced by the same countries in the immediate aftermath of the global financial crisis ($26.7 billion). The drastic and much larger drop in net portfolio flows from developing countries, compared to other recent crisis episodes, is also clearly visible in Figure 2.b below, that includes additional country data available for the Covid-19 crisis period.[3]

Figure 1.a **Net portfolio flows, selected developing countries: Debt and equityPost-GFC and onset of COVID-19 crisis**

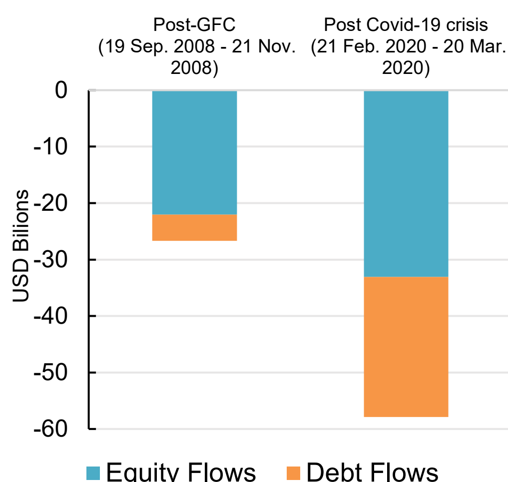
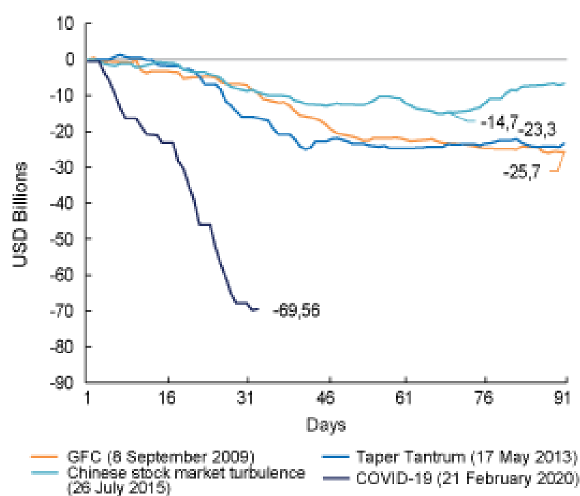


Figure 1.b **Net portfolio outflows from selected developing countries: Total flows after recent crisis**



Source: UNCTAD secretariat calculations based on *IFF Daily Emerging Market Portfolio* database.
Note: Figure 1.a includes: Brazil, India, Indonesia, Philippines, Republic of Korea, South Africa, Thailand and Turkey for both data points. Figure 1.b also includes China, Mexico, Pakistan, Qatar, Saudi Arabia, Sri Lanka and Vietnam.

Concomitantly, the spreads on developing country bonds have been rising sharply (Figure 2), while the value of currencies against the dollar (Figure 3) have dropped significantly since the beginning of this year; and again, in both cases equal to or faster than the early months of the global financial crisis.

[3] On the likely drop in FDI flows, see https://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=2313

Figure 2.a **ICE BofA Emerging Markets Corporate Plus Index Effective Yield, in the days after the main shock** (annual in percent)

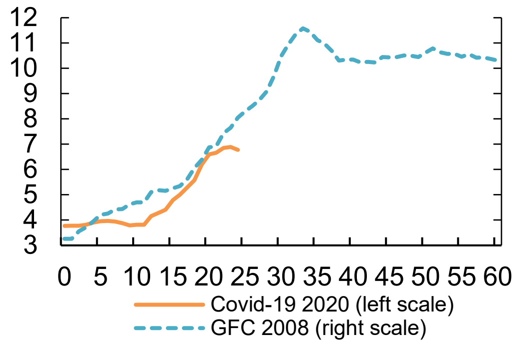
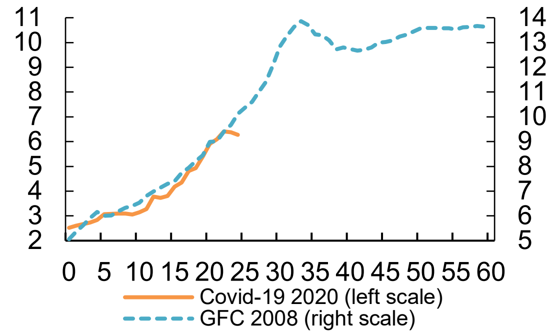


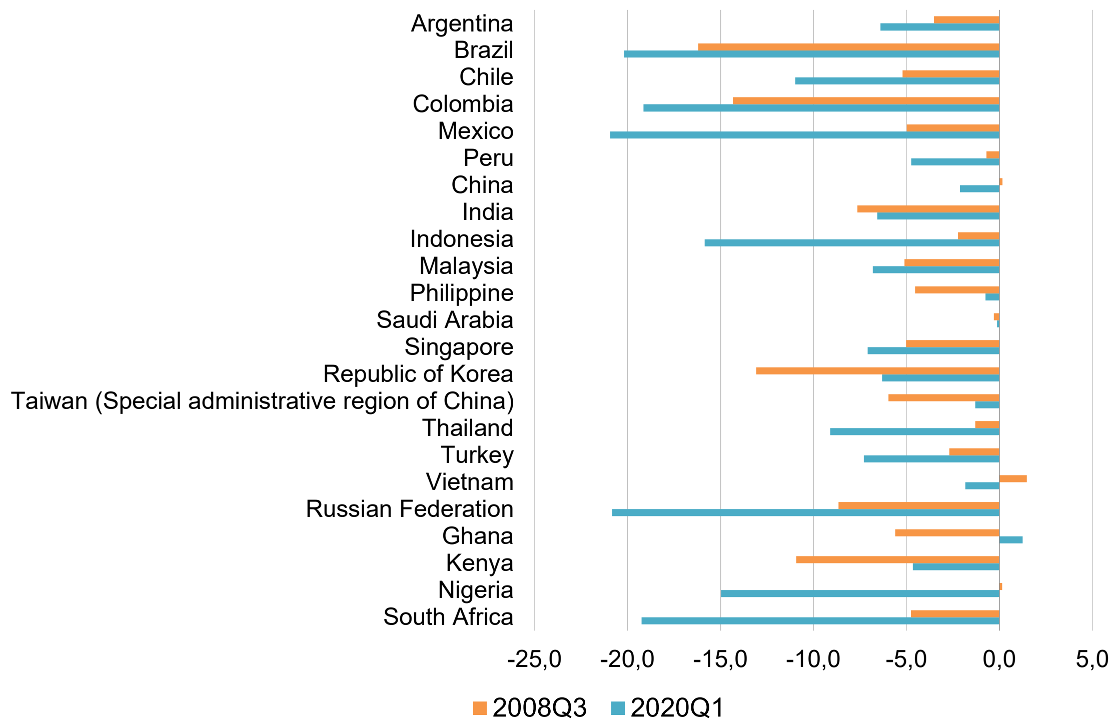
Figure 2.b **ICE BofA Emerging Markets Corporate Plus Index Option-Adjusted Spread, in the days after the main shock** (annual in percent)



Source: FRED, day zero is Friday, 12/Sep/08, for the GFC,and Friday, 21/Feb/20, for the Covid-19 shock.
Note: calculated over US Treasury curve.

Commodity prices have also dropped precipitously since the crisis began (Figure 4). A fall in oil prices, which would be expected from a drop in global demand, has been amplified by disagreements among the main producers on how to deal with this, with Brent crude falling 63 percent in the year to date. In the last 25 years, similar declines occurred only after the Global Financial Crisis (GFC) of 2008 (figure 4).

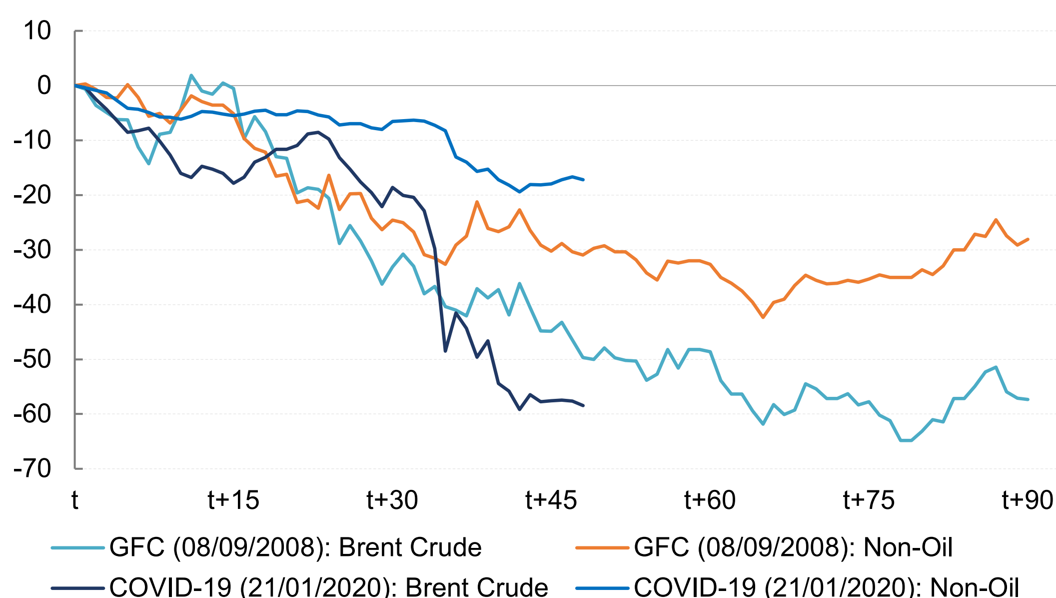
Figure 3 **Currency movements against the dollar, 2008Q3 vs 2020Q1** (Percentage)



Source: UNCTAD secretariat calculations based on *Thomson Reuters Eikon* database.
Notes: Negative values refer to a depreciation of the domestic currency against the dollar. Data for 2020Q1 go until 25 March.

When other commodities are added to the analysis, the overall price decline has been 37 per cent this year, with the other major falls concentrated in metals (with some notable exceptions) and mineral products. The reduction in the price of agricultural commodities has, on average, been smaller but with some notable exceptions (see also Table 1).

Figure 4 **Commodity Prices**
(Percent change: "t + x working days" vs. "t")



Source: UNCTAD secretariat calculations based on Thomson Reuters Eikon.

This time things *are* different

The economic fallout from the Covid-19 shock is ongoing and increasingly difficult to predict but there are clear indications that things will get much worse for developing economies before they get better.

First, the full effects of the health crisis have yet to hit many developing countries, and we have yet to reach the “end of the beginning” of the economic crisis in the advanced economies. Following the collapse of Lehman Brothers in September 2008, the global economy registered 5 consecutive quarters of negative growth, albeit at a decelerating rate after the second quarter of 2009; even if the massive stimulus packages now being implemented prevent a long period of depression, they will not, as already suggested, avert a recession in the global economy this year.

Second, many of the conditions that produced a sharp bounce back in developing countries after 2010 are no longer present or a good deal weaker. China’s massive stimulus in 2009 and rapid return to double digit growth had strong positive effects on demand for the exports of developing countries while the search for yield by Northern investors operating under the loose monetary policy adopted by leading Central Banks heightened their appetite for risky assets, producing a rapid rebound in capital inflows in emerging and other developing countries. Moreover, confidence in the developing world was boosted by expanding South-South trade and financial links that had begun before the crisis hit, encouraging the idea that developing countries had “decoupled” from the economic troubles of developed countries. These conditions are unlikely to be repeated this time around. In addition, weakening state capacity, diminishing fiscal space and

a rise in illicit financial flows over the past decade, place further constraints on effective recovery strategies in many developing countries.

Third, the strong recovery in developing country trade that occurred in 2010 seems less likely this time. Even if the damage to global supply chains is not irreparable, as lead firms recover from the crisis they will likely have to rethink their business model, including fewer links in these chains, and with more that are closer to home. Moreover, China has steadily diminished its dependence on external suppliers in its chains through an increase in domestically produced intermediate products. At the same time, there has been too little diversification of economic activity in many developing countries over the past decade – with greater commodity dependence in many countries -- leaving them more exposed than ever to new shocks and disturbances.

Fourth, the current fall of commodity prices has started from a lower value compared to what happened in the GFC when the world economy was at the peak of the "super commodity cycle" and appears to be more broad based. Commodity prices have been well off their post-recovery highs since the price slump in 2016 but it seems unlikely that there will be the same kind of pick up in prices seen between 2009 and early 2011 which was well ahead of the recovery in global output (see Table 1).

Fifth, new vulnerabilities have emerged that are likely to hold back growth. Emerging economies, in particular, have seen a rapid build-up of private debt in reserve currencies and increased penetration of their markets by non-resident investors, foreign banks, and other financial institutions, as well as allowing their own residents to invest more freely abroad. There has also been a strong shift in the ownership of central government debt, including public external debt, from official to private creditors and shadow-banking actors. These trends heighten developing countries' external vulnerabilities and entail large transfers of resources to advanced economies through various financial channels. As argued extensively in previous UNCTAD reports, even with the exceptionally low interest rates seen since the financial crisis, the resulting wave of debt accumulation was looking more and more fragile before the coronavirus crisis hit. The greater presence of foreigners in bond and equity markets has, moreover, increased the potential instability of exchange rates and further exposed domestic financial markets to the vagaries of global risk appetite and liquidity conditions.

Finally, developing countries' ability to build up international reserves as a buffer against macroeconomic shocks has been weakening. In the aftermath of the global financial crisis, developing countries' international reserves increased steeply, precisely in response to an evident need for "self-insurance" in a volatile global economic environment. However, since the onset of the commodity price downturn in 2012, reserve holdings, while still high by historical standards, have fluctuated widely, reflecting multiple pressures on developing countries' ability to maintain high reserve holdings, such as commodity price downturns and growing debt and financial vulnerabilities. Given the massive expected impact of the Covid-19 crisis, reliance on such self-insurance is not an option, with reserves likely being drained very fast.

Table 1 **World primary commodity prices, 2017–2020**
(Percentage change over previous year)

	2017	*2018*	*2019*	*2020**
All commodity	11,1	-15,4	16,5	-37,3
Energy	12,3	-20,9	24,2	-55,1
Industrial metals	31,0	-19,0	1,5	-18,4
Aluminum	34,1	-19,0	-1,9	-15,1
Copper	30,8	-17,5	3,4	-21,3
Lead	23,8	-18,6	-4,8	-14,6
Nickel	27,5	-16,4	31,4	-19,5
Zinc	29,6	-25,6	-8,0	-19,4
Precious metals	12,9	-2,9	18,5	5,0
Gold	13,7	-2,1	18,9	7,3
Silver	7,2	-9,4	15,3	-17,0
Platinum	3,6	-14,7	22,1	-23,7
Agriculture	-3,0	0,6	6,3	-6,8
Cocoa	-11,0	27,7	5,1	-11,5
Coffee	-7,9	-19,3	27,3	0,2
Corn	-0,4	6,9	3,4	-10,1
Cotton	11,3	-8,2	-4,4	-22,6
Soybeans	-4,2	-6,9	6,8	-7,7
Sugar	-22,3	-20,6	11,6	-15,0
Wheat	4,1	16,8	7,7	3,6
Livestock	7,2	-3,0	5,0	-14,7

Source: UNCTAD Secretariat calculations, based on GSCI spot indices.
Note: Data for 2020 refer to year-to-date growth rate as of 25 March 2020.

The looming financing gap in developing economies

The analysis of the impact of the Covid-19 shock has been mostly concentrated on China and advanced economies, since they were initially more affected by the pandemic, account for three-quarters of world output and have the monetary and fiscal policy space to respond. However, since two-thirds of the world population live in the (remainder of the) developing world, the responses to the current shock must include dedicated and actions for developing countries, at all income levels.

In general terms, there are three main transmission mechanisms or channels through which the Covid-19 shock can be expected to increase financial pressures on developing economies over the coming months.

The first channel is the pressure on government budgets from the public health crisis. The social distancing necessary to stop the contagion has already led to economic shutdown in many developed and developing countries affecting the majority of the world's population. A sharp, sudden fall in employment is already happening. While developed countries have the administrative capacity and (generally) the fiscal space to buttress their social protection systems and protect private incomes, in developing countries sharp contractions of incomes are all but inevitable along with falling fiscal revenues. Tighter fiscal space and weaker healthcare and social

protection systems expose developing countries to higher human and financial toll while limiting their ability to respond, triggering a potentially dangerous vicious circle. Moreover, with fast-increasing need for imports of specialized goods and services to deal with the health crisis the balance of payments constraint can only expect to tighten further.

The second channel is international trade. Even after considering implementation of the effective $1.4 trillion stimulus by advanced economies and China, a rapidly slowing growth in these countries will take place through 2020. This will mean significantly lower demand for exports for other developing economies. The losses in export volume will be compounded by the sharp falls in energy and commodity prices, which still make up most of the goods that many developing countries export. Altogether, we project that developing countries as a whole (excluding China) will lose nearly $800 billion in terms of export revenue in 2020. Such a drastic fall in their foreign exchange earnings will add to the challenges already posed by currency depreciations vis-à-vis the US dollar. While imports will contract, by an estimated $575 billion, the overall drop in the trade balance of around $225 billion is not without consequences for their development needs, their structural transformation plans and their ability to generate output and capacity to continue to face external financial commitments. Moreover, other items on the current account, such as remittances, royalty payments and profit outflows are likely to add to the financing difficulties facing many developing countries over the course of the coming year.

The third channel is financial. The flight to safety has, as noted earlier, already caused record capital outflows from emerging economies, triggering large currency depreciations against lead currencies and widening spreads. In countries with a high exposure to foreign debt, be it private or public, these trends put enormous pressure on their debt sustainability, by undermining future access to refinancing outstanding external debt obligations while driving up their value in foreign currency. This comes against a background of a systematic build-up of financial and debt vulnerabilities in many developing countries over the past decade. Total developing country debt stocks stood at 193 per cent of their combined GDP at the end of 2018, the highest on record, compared to just over 100 per cent in 2008.

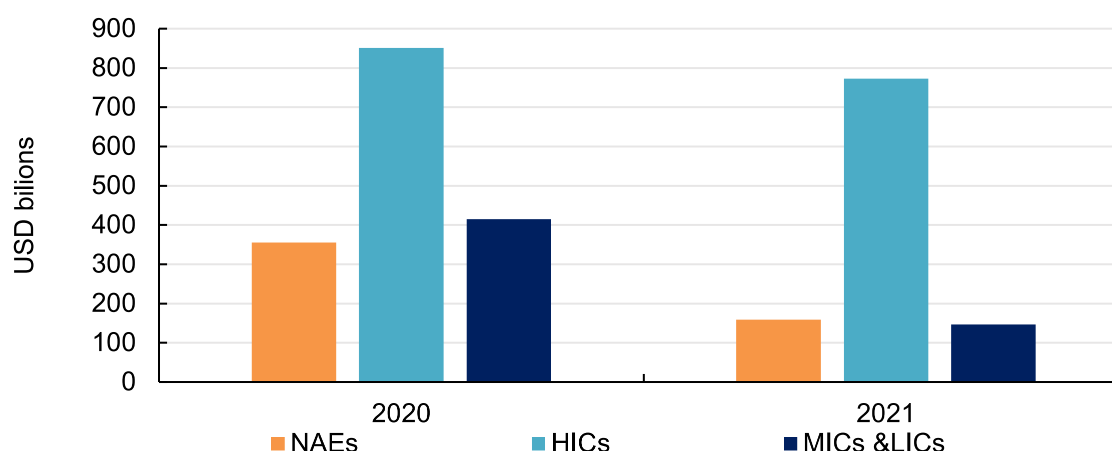
In addition to rising debt servicing costs since 2012, developing countries also already face a wall of repayments due on foreign-currency denominated public debt over this year and the next. As Figure 5 below shows, the total amount of sovereign debt repayments due at the end of 2021 is $2.7 trillion ($1.62 trillion in 2020 and $1.08 trillion in 2021). Of this, $562 billion are due for repayment by governments in low- and middle-income countries, with the bulk of this amount due this year ($415 billion in 2020 and $147 billion in 2021). In "normal" times, much of this debt would be rolled over, adding to future debt burdens but providing vital breathing space to honor overall obligations. But with sudden stops to external refinancing possibilities, suspending sovereign debt repayments due over this and the next year, at the very least for low- and middle-income developing countries, is key to averting immediate and wide-spread debt crises. Clearly, the amounts that would be involved in suspending sovereign debt repayments in poorer developing countries are small change compared to the economic rescue packages hurriedly put together across the developed world.

What is to be done?

Advanced economies have embarked on a dramatic change of policy direction in response to the crisis. Measures that were unthinkable just a few weeks ago have been embraced and implemented in response to the scale of the crisis. So far discussion of what developing countries should and could do has, by contrast, been limited, particularly when it comes to international support.

In the current dollar-centric global system, the United States' Federal Reserve can extend its role as lender of last resort beyond the country's borders but it currently does so in a strategic way which favours a select group countries. As of 19 March, the Federal Reserve has currency swap programmes with nine Central Banks (enabling these to provide dollars to their own banking systems that lend and trade in dollars), including only three developing countries - Brazil, Mexico and Singapore. This comes as the role of the dollar in the developing world has been increasing since the global financial crisis, largely due to developing countries' growing recourse to international financial markets to meet external financing needs. Thus, at the end of 2007 and the peak of the pre-crisis boom, developing countries' outstanding international debt securities - such as bonds, asset-backed securities and commercial papers issued by their governments and firms - denominated in dollar stood at $840 billion, or 70 per cent of the total amount of $1.2 trillion. By end 2019, this figure had risen to $3.36 trillion, or 80 per cent of the total amount of developing countries' outstanding international debt securities of no less than $4.2 trillion.[4] While advanced country governments are preparing to send checks to their citizens and open emergency credit lines for their companies, this clearly is not an option open to most developing countries which are highly dependent on access to US dollars and which lack their own financial infrastructure and financial firing power to follow suit.

Figure 5 **Redemption schedules for public external debt in developing countries, bonds and loans, 2020 and 2021**



Source: *UNCTAD secretariat calculations based on World Bank QEDS and IFF Global Debt Monitor.*
NAEs (new advanced economies): Hong Kong (China), Russian Federation, Singapore, Republic of Korea, Turkey, Ukraine. **HICs (high income developing countries):** Argentina, Brazil, Chile, China, Colombia, Lebanon, Malaysia, Mexico, Saudi Arabia, South Africa, Thailand, UAE; **MICS & LICs (middle-and low-income developing countries)**: Egypt, Ghana, India, Indonesia, Nigeria, Pakistan, Philippines, Burkina Faso, Ethiopia, Madagascar, Nepal, Rwanda, Sierra Leone, Uganda, Yemen, Rep., Bangladesh, Belize, Bolivia, Cameroon, Cote d'Ivoire, Djibouti, Fiji, Guatemala, Honduras, Kenya, Nicaragua, Papua New Guinea, Paraguay, Solomon Islands, Tonga.
Notes: Data refer to sovereign debt for NAEs and HICs and to public external debt for MICs and LICs.

It is therefore a matter of immediate urgency for the international community to co-ordinate appropriate economic rescue packages with a more global reach to address the looming financing gap which many developing countries are now imminently facing. These would have to include, as a minimum, the following measures:

[4] Bank for International Settlements Debt Securities Statistics (by nationals).

First, a coordinated global response to liquidity shortages to address immediate financing needs. While the recent pledge by the Group of 20 to inject $5 trillion into the global economy to limit economic losses from the Covid-19 crisis is welcome, how effective any such rescue package will be, and how much of it will reach developing countries, remains to be seen and depends on specific measures. Furthermore, the IMF has signalled that it is willing to fully deploy its current $1 trillion lending capacity to help deal with the crisis. However, not only is this likely to prove insufficient, but current lending facilities and financing instruments are complex, tied to inappropriate conditionalities under the circumstances and therefore difficult to access quickly, in particular for developing countries. While the IMF has promised flexibility in this regard, an additional and faster avenue to address, at the very least, current liquidity shortfalls is through a much more expansive use of ***Special Drawing Rights*** (SDRs), the IMF unit of account and an international reserve asset (see Box 1). Under current arrangements, this instrument suffers from the bias in the IMF's quota system that continues to heavily favour advanced countries. Even so, a serious step towards alleviating liquidity constraints, in particular in low-and middle-income economies, would be to ensure that around 730 billion SDRs ($1 trillion at the current exchange rate) reaches the international reserve accounts of developing countries fast. This could be achieved through a new allocation of SDRs and an IMF "designated" reallocation of current and new but unused SDRs from advanced countries to poorer developing economies. The required new allocation of SDRs would, no doubt, have to be multiple times that agreed in 2009 (of 183 billion in SDR or the equivalent of $287 billion at the time), depending on developing country liquidity needs and options for a "designated" reallocation of existing and newly allocated SDRs. But this would be an appropriate response to the scale of the crisis and the plight of large numbers of developing countries.

Second, ***capital controls*** should be endorsed by the IMF as a necessary, permanent and fully legitimate part of any policy regime and wherever appropriate introduced to curtail the surge in outflows, to reduce illiquidity driven by sell-offs in developing country markets, and to arrest declines in currency and asset prices. Implementation should be coordinated by the IMF to avoid stigma and prevent contagion, and who, in cooperation with other appropriate international bodies, should also be tasked with lending the technical support needed to ensure their effectiveness and extending advice on complementary measure needed to deal with related disruptions.

Third, even if large liquidity injections to developing country reserve accounts are critical to staving off financial and economic meltdowns and serial sovereign defaults in developing countries, it will be important to ensure that the medium-to-longer term economic fallout from this global health crisis also does not result in destructive and wide-spread developing country debt crises. One such measure are ***temporary standstills*** on debt service payments, or a formal or informal agreement between a debtor and one or more of its creditors to suspend these payments for a given period of time to allow debtors to propose restructuring plans. During this time creditors cannot seek legal remedies, a critical provision to keep non-cooperative and litigious creditors (or so-called vulture funds) in check. While there has been ongoing debate about the institutional avenues to govern temporary standstills, UNCTAD has long argued that such standstills should be triggered by the unilateral decision of debtor countries to declare their need to freeze debt repayments temporarily, and should subsequently be sanctioned by an independent panel of experts, rather than creditor organisations. While there may be little time, in the current circumstances, to create new international bodies to govern temporary standstill procedures, this would be just one of many extraordinary measures taken with unusual speed over the past months.

Fourth, and in addition to temporary standstills as a kind of emergency break, new ***debt relief programmes*** need to be agreed on as soon as possible. On 25 March, the World Bank and the IMF called on all official bilateral creditors to suspend debt payments from the world's 76 poorest

economies, currently in receipt of support from the International Development Association (IDA). While a first tentative step in the right direction, more systematic, transparent and co-ordinated steps towards writing off developing country debt, based on need rather than bargaining power, are critical. As pointed out, the wall of debt repayments about to hit a large number of developing countries is unsustainable. In addition to sovereign debt repayments due until the end of 2021 (see above), another 42.75 trillion is scheduled for repayment from 2022 through to 2024, of which 4482 billion are owed by low- and middle-income country governments. For now, African Finance ministers have indicated that a waiver of all interest payments on their debt, estimated at 444 billion for 2020, and a possible extension to the medium-term would help to provide immediate fiscal space and liquidity to their governments. However, unless more comprehensive debt relief programmes are agreed now, future redemption schedules will fast look very much worse than is the case at present. It should not be a matter of over-stretching global economic governance capacities, to design an immediate debt relief package for stricken developing countries, beginning with those already in default and, according to IMF debt sustainability assessments, at high risk of debt distress. A measure of ambition, which should at least be matched in the face of the current crisis, is provided by the cancellation in 1953 of half the German debts accumulated over the previous three decades and future payments made contingent on export earnings.

Fifth, Official Development Assistance (ODA) must be ring-fenced in all donor countries. Despite a majority of donors having routinely missed agreed ODA targets in the past, and despite ODA flows being spread ever more thinly across additional donor-determined objectives, ODA remains a vital source of external financing for the poorest of developing countries. Over the decade since the financial crisis an additional $2 trillion would have reached developing countries had the 0.7 per cent (of global national income) ODA target been met by DAC members. This, therefore, is the time, for donor countries to, finally, honour their collective commitment and deliver ODA to developing countries in full and unconditionally. As an extraordinary measure given the immediate situation, channelling a significant amount of the missing amount of ODA – say one quarter of that total – into a ***Marshall Plan for Health Recovery*** would be a fitting way to demonstrate the international solidarity needed to mitigate the crisis in developing countries.

As the health pandemic is brought under control and economic shocks dissipate, a more profound reevaluation of the multilateral system -- promised but not delivered in 2009 -- will be needed to ensure that resilience and fairness become integral characteristics of our more interdependent world.

The current shock, coming a decade after the GFC, the rampant inequalities and the fast-accelerating environmental destruction from rising global temperatures (both land and sea), are the wake-up call that should push all governments and international institutions to mobilize against the stresses and fractures that have produced an increasingly fragile and anxious world. Immediate steps in response to the crisis should therefore signal a new beginning for global governance.

Box 1: Special Drawing Rights to the Rescue – especially for developing countries

In the immediate aftermath of the global financial crisis, IMF member states agreed to a new allocation of Special Drawing Rights (SDRs) for the first time in almost 30 years. At $ 183 billion SDRs (or $ 287 billion), this amounted to a more than eight-fold increase over previous allocations taken together.

Special Drawing Rights (SDRs) are the IMF's unit of account and a potential claim on holdings of freely usable and available international currencies. They are best thought of as a virtual reserve asset created by the IMF and valued daily as the weighted linear combination of the market prices of five international lead currencies. SDRs are allocated to IMF member states participating in its SDR department in line with their IMF quotas. Member states can then make use of SDRs as a means of payment between them and to obtain hard currency. In addition, IMF "designations" can call upon surplus countries to acquire SDRs from deficit countries to help provide them with needed liquidity in hard currency. According to the IMF's Articles of Agreement the aim of SDR allocations (or cancellations) is "to meet the long-term global need […] to supplement existing reserve assets" so as to "to avoid economic stagnation and deflation as well as excess demand and inflation in the world".

In order to ensure that around 730 bn in SDRs (or $ 1 trillion) can be put into place to alleviate developing countries' liquidity constrains over the coming months there are two options: The first option assumes that the current quota system remains in place. In this case, for 730 bn SDRs to reach developing countries' reserve accounts, the overall new allocation of SDRs would have to amount to between 2 to 3.5 trillion in SDRs (or $ 3 to 5 trillion at the current exchange rate). This is because, under the current quota regime, only around 10 per cent of the total would go to all lower- and middle-income developing countries taken together and just short of 25 per cent, if larger developing countries and China are included. In 2009, of the 183 billion SDRs allocated, only around 12 billion went to African countries, but even so they made a huge difference. If the IMF also made use, as it last did in 1987, of its "designation" powers to ensure that surplus economies acquire SDRs from deficit countries to facilitate their access to hard currency, this could reduce the total amount of new allocations required. At the lower end of estimations, a new allocation of SDRs of 2 trillion (or $ 3 trillions) would amount to around an 11-fold increase of the SDR allocations the rate of increase in SDR allocations implemented in 2009.

The second option would be to de-link a one-off allocation of SDRs from the quota system, as an exceptional measure. Any new allocation of SDRs would then include 730 billion SDRs for developing countries, in addition to what is considered necessary for other economies, considerably reducing the overall new SDR allocation required under the first option. In view of the general agreement that the current crisis is likely to affect developed and, in particular, developing countries more severely than the global financial crisis, neither option should be unthinkable.

In the medium to longer run, it will be vital to ensure that SDR allocations become a routine tool of IMF operations, rather than a last-resort reserve-pooling arrangement in exceptional circumstances, to address systemic and structural imbalances in the global economy. As Keynes noted, in demanding times the difficulty lies not so much in developing new ideas as in escaping from old ones.