Will the BRICS Bank and Fund boost Global South?

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THE 6th Summit of the BRICS took place last week in Fortaleza, Brazil with two landmark decisions, viz., to form a BRICS Bank and a Contingency Reserve Arrangement (CRA or the BRICS Fund) and bring them into operation by 2016.Initiated in mid-2009, BRIC became BRICS in 2010 when South Africa joined Brazil, Russia, India and China to form a grouping of 5 large emerging economies. The key objective of the grouping was to have a bigger say in the global financial order which is currently dominated by Western countries. BRICS represent 40% of the global population,18% of global trade, and possess US$ 4 trillion in combined foreign reserves.

The large foreign reserves of BRICS and many developing economies in Asia have been mostly invested in the US Gilt-edged Securities and Sovereign Wealth Funds over the years. Despite the low yield in such securities and funds, the bulk of the reserve surpluses of emerging and developing economies have been invested in them mainly due to the strength and international standing of the US dollar.Had these reserves been invested in emerging and developing economies, they would have not only bridged the massive infrastructure deficit of those countries but also uplifted millions of people out of poverty.

For instance, the Economics and Social Survey for Asia and the Pacific Report 2010 produced by the ESCAP has estimated that if US$800 billion per annum was allocated to the Asia-Pacific region, the infrastructure deficit could have been covered in the region in a couple of years. ESCAP in fact, argues that the rate of return on investing part of the reserves in the region would have been higher than the returns from the US market, and for this purpose only 5% of the US$ 5 trillion reserves in the region could have been used to create an Infrastructure Fund. Such thinking influenced the Chinese and it led to China proposing to set up an Asian Infrastructure Investment Bank on similar lines to Japan taking the initiative to form the Asian Development Bank in 1966.

Such thinking also influenced the BRICS leaders and they were convinced that the emerging and developing economies had enough savings and foreign reserves to establish a development bank that could provide funds for infrastructure projects in these countries and in 2011 the need for a BRICS Bank was mooted. The decision at the 6th BRICS Summit was to aim at US$ 100 billion total capital for the bank with US$ 50 billion made available as start-up capital by the 5 countries at the beginning. The bank will be located in Shanghai with an Indian as the Chairman.

It has been estimated that close to US$ 1 trillion is required per annum to meet the infrastructure deficit in emerging and developing countries. The existing local, regional, and multilateral banks cannot meet this requirement and the new BRICS Bank will be able to supplement the existing banks. The BRICS Bank will benefit from the experience of the currently functioning development banks like the Chinese Development Bank, Brazilian BDNES, South African Industrial Development Corporation, etc. It will not only complement the existing network of banks but also have the late-comer advantage.

The CRA was very much prompted following the outflow of capital from emerging and developing country markets (after mid-2013) which was triggered by US scaling back on monetary stimulus known in US jargon as “tapering Quantitative Easing”. The CRA will be a currency swap arrangement allowing for emergency support to BRICS countries experiencing a balance of payment crisis. The CRA will be established with US$ 100 billion with China contributing US$ 41 billion, South Africa – US$ 5 billion, and others filling in the rest with US$ 18 billion each. CRA will have no involvement with the IMF unlike the Chang Mai Initiative Multi-lateralization where 30% of member's quota is accessible (when having an IMF programme) with IMF concurrence. The CRA will complement the IMF.

The launch of the BRICS Bank and CRA will be concerted steps for reshaping the Western dominated international financial system. It will be the first step to challenge the domination of the US influenced World Bank and the IMF and the US dollar. It may be worth recalling that the attempt made by Japan soon after the East Asian Financial crisis to form an Asian Monetary Fund was shot down by the IMF and the US Treasury. Such tacticswill become increasingly difficult with the BRICS.

The establishment of two large BRICS financial institutions will also pave the way for BRICS advancing reforms in international financial architecture and tilting it in favour of emerging and developing countries as their voice is still weak in the G-20 dialogue. This weakness is amply demonstrated on the lack of progress in IMF quota and governance reforms which have been in the global debate for some years now.

Needless to say, many questions still remain unanswered. Now that the BRICS Bank is on the pipeline, will China give up its idea of establishing the Asia Infrastructure Investment Bank? Will the BRICS Bank give large loans at a more concessional rate than the World Bank? How much more 'policy space' will the CRA provide compared to the IMF's more liberal conditionalities since of late after the global economic crisis? To what extent will BRCIS represent the interest of all developing countries? Already, Indonesia, Turkey, Argentina, Egypt, Iran, Nigeria and Syria have expressed an interest in joining BRICS. Will they be taken in?

We may find answers to these questions once the two BRICS initiatives start gathering momentum. At least for now, all developing countries will feel that their interests will be represented more effectively by the BRICS in the global financial dialogues. Only time will tell whether this will be the case.

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