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Trends in Global Finance: The New Development (BRICS) Bank

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Trends in Global Finance: The New Development (BRICS) Bank

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I. Introduction

This Critical Essay will discuss the formation of the New Development Bank (NDB or the "Bank") by the BRICS nations, i.e., Brazil, Russia, India, China and South Africa. This discussion will critically examine the creation of the NDB in terms of its policy implications in leading up to the formation of the Bank and in its potential downstream consequences. Since the inception of the NDB is so new, this essay will err on the side of raising questions rather than attempting to resolve them at this stage. In furtherance of this objective, the following discussion will review: (1) a brief history giving rise to the creation and formation of the NDB; (2) the structure, operation and mission of the Bank; (3) the impact of the Bank on the hegemony of the U.S. dollar and on U.S.-led economic sanctions regimes; and, finally, (4) the change in the global financial architecture heralded by the NDB, and its potential impact on international development in general.

At the outset, it may seem that the amalgamation of the BRICS nations into a group, let alone a bank, is haphazard and ill-fitting. It was a concept developed by Jim O'Neill, a former economist at Goldman Sachs.[1] In that analysis, Mr. Goldman predicted that in 2001-02, real Gross Domestic Product (GDP) growth in large emerging market economies, namely the BRICs (Brazil, Russia, India and China), will exceed that of the G7. Since that time, the concept of rapid economic growth in the BRICs as a unifying principle has burgeoned, ultimately resulting in conferences, summits, new political and trade alliances, and now a new bank. In the view of Mr. Goldman, however, the inclusion of South Africa in this group is a mistake since its GDP is too low in comparison with the other

* This essay summarizes and expands the remarks made by the author at the Loyola University Chicago International Law Colloquium 2015 held on April 29, 2015. Professor Rumu Sarkar is a member of the Loyola University Chicago Advisory Committee (Emerita) for its PROLAW program, located in Rome, Italy, which is designed to provide a Masters of Law degree in international development law issues. Professor Sarkar is also the General Counsel to Millennium Partners, an international development consulting firm located in Charlottesville, VA.

[1] Jim O'Neill, *Building Better Global Economic BRICs*, Goldman Sachs Global Econ Paper No. 66, November 30, 2001.

members.[2] Nevertheless, South Africa was added since the other members felt that the continent of Africa needed to be represented in this group and in its new banking venture.[3]

Certainly, there are obvious distinctions among the BRICS members who have diverging and, in some cases, conflicting interests. While India, Brazil and South Africa are democracies, Russia and China are not. Russia's economy is based on the export of natural resources, whereas China's imports much of its resources and exports manufactured products.

In contrast, India's economy depends heavily on technology and services, and the economies of South Africa and Brazil, also export-driven, are a blend of the above. China and India have long-standing territorial disputes that remain unresolved,[4] and China often vies for economic power with the United States and for political power with Russia. China and Russia are both permanent members of the UN Security Council, but India, also a nuclear power, is not despite its repeated and strenuous attempts to join over the past decade or more.[5] Despite these and many other differences in population, history, languages, and more, the BRICS nations have shown a new resolve in addressing the perceived deficiencies in the current global financial architecture. Their response is both new and innovative, and time alone will reveal whether this partnership will be successful and enduring.

II. History as Prologue: IMF Reforms as a Backdrop to the Formation of the NDB

The second week of July 2014 marked the 70th anniversary of the signing of the Bretton Woods Agreement that established the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (the "World Bank") in Bretton Woods, New Hampshire in 1944. On July 15, 2014, 70 years later, the BRICS announced the formation of the New Development

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[2] *See, e.g.*, Nima Elbagir & Teo Kermeliotis, *South Africa an Economic Powerhouse? Nowhere Near, says Goldman Exec*, CNN (Apr. 5, 2011), http://edition.cnn.com/2011/BUSINESS/04/05/jim.oneill.africa.bric/ (noting that the Chinese economy is 28 times larger than that of South Africa's according to *The Economist*); *see also*, *The BRICS Bank: An Acronym with Capital*, ECONOMIST (July 19, 2014), http://www.economist.com/news/finance-and-economics/21607851-setting-up-rivals-imf-and-world-bank-easier-running-them-acronym [hereinafter, The BRICS Bank].

[3] J.P.P., *Why is South Africa Included in the BRICS?* ECONOMIST (Mar. 29, 2013), http://www.economist.com/blogs/economist-explains/2013/03/economist-explains-why-south-africa-brics.

[4] Michael Forsythe, *China Protests India's Leader Visit to Disputed Border Area*, N. Y. TIMES (Feb. 23, 2015), http://www.nytimes.com/2015/02/23/world/asia/china-protests-india-leaders-visit-to-disputed-border-area.html?_r=0. *See generally India China Border Dispute*, globalsecurity.org, http://www.globalsecurity.org/military/world/war/india-china_conflicts.htmhttp://www.globalsecurity.org/military/world/war/india-china_conflicts.htm; Shannon Tiezzi, *Can India and China Overcome Their Border Dispute?*, THE DIPLOMAT (Sept. 19, 2014), http://thediplomat.com/2014/09/can-india-and-china-overcome-their-border-dispute/.

[5] William Petroff, *What are the Obstacles Faced by India When Becoming a Permanent Member of the UN Security Council? How Can India Tackle It?*, QUORA, http://www.quora.com/Why-is-India-not-a-permanent-member-of-the-UN-Security-Council (last updated Sept. 17, 2015); *see also* Neelam Deo & Karan Pradhan, *Should India Give Up on the UN Security Council?*, THE DIPLOMAT (Nov. 19, 2014), http://thediplomat.com/2014/11/should-india-give-up-on-the-un-security-council/.

Bank and the Contingent Reserve Arrangement (CRA) at its sixth annual summit held in Forteleza, Brazil. The NDB is designed to finance infrastructure and sustainable development projects, mirroring the function of the World Bank. The CRA was created to make foreign reserves available to provide balance of payments support for BRICS members in financial difficulty, mirroring the function of the IMF. Since the IMF and the World Bank are already well-established and functioning multilateral bodies that the BRICS are all members of, why were the NDB and CRA created?

A Deeper Dive. IMF membership is determined by a quota system whereby each member country is assigned a quota, or monetary contribution, that is designed to reflect the size of the member country's relative size as measured by its GDP. These quotas have not been revised much since the inception of the IMF, and no longer reflect the relative economic size or power of its member countries.[6]

For example, the BRICS possess 11% of the IMF's votes but account for more than 20% of global economic activity.[7] In other words, the four major BRICS economies, Brazil, China, India and Russia, have a combined share of the world GDP of 24.5%, but have only 10.3% of the IMF's votes.[8] In contrast, the four largest European economies, France, Germany, the UK and Italy, represent 13.4% of the world GDP, but have 17.6% of the IMF's votes.[9] China makes up approximately 10% of world GDP, but has 5% of the votes.[10] The U.S. at the time of the Bretton Woods conference in 1944 held 33% of the IMF's votes, and now holds 17% of the IMF votes,[11] the largest share held by any country.[12] We will explore the implications of this below.

Reforming IMF's Quotas System. The political quest to reform the IMF quota system began in earnest with the Bush Administration in 2008, and was further solidified by President Obama's commitment to IMF reform at the G-20 summit meeting held in Seoul, South Korea in November 2010.[13] The Seoul IMF reform package contained three essential elements:

(1) Doubling the IMF quotas with a corresponding reduction in the size of the commitment to the New Arrangements to Borrow (NAB) for certain coun-

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6 Jon Hartley, *The BRICS Bank Born Out of Politics*, FORBES (July 28, 2014), http://www.forbes.com/sites/jonhartley/2014/07/28/the-brics-bank-is-born-out-of-politics/.

7 Barry Eichengreen, *Do the BRICS need their own Development Bank?* THE GUARDIAN (Aug. 14, 2014), http://www.theguardian.com/business/2014/aug/14/brics-development-bank-imf-world-bank-dollar.

8 Robert Wihtol, *Whither Multilateral Development Finance?*, 10 (ADB Institute, Working Paper No. 491, 2014), *available at* http://www10.iadb.org/intal/intalcdi/PE/2014/14541.pdf.; *see also* Hartley, *supra* note 6.

9 *Id.*

10 Hartley, *supra* note 6.

11 *Id.*

12 Nansel Stobdan & Rucheta Singh, *The BRICS Bank and Its Prospective Place in the World Economy* 4 (Dec. 1, 2014), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2538710.

13 Edwin Truman, *IMF Reform is Waiting on the United States*, 3 (Peterson Inst. for Int'l Econ., Paper No. PB14-9, Mar. 2014), http://www.piie.com/publications/pb/pb14-9.pdf.

tries, most notably the United States, resulting in a reallocation of the quotas and respective voting shares;

(2) An amendment to the IMF Articles of Agreement permitting an all-elected executive board with a view to reducing and consolidating European representation on the IMF Executive Board. Currently, five nations with the largest quotas are allowed to appoint an executive director, namely, the United States, Japan, Germany, France and the United Kingdom;

(3) The reduction of the representation of advanced European nations on the 24-person IMF executive board.[14]

In essence, about 6% of the IMF's shares would shift to emerging economies, in particular, China, Brazil and India. Additionally, two seats on the IMF's Executive Board that are currently held by European countries would change over as well.[15]

The Seoul package was formally adopted by the IMF board of governors in December 2010,[16] with passage of the reform package expected from its members by January 2014.[17] As of February 25, 2014, 158 of the 188 IMF members with 78.7% of the votes had consented to the increases of their quotas, representing a doubling of the existing IMF quotas.[18] However, since the United States has 16.75% of the vote, its approval of the amendment to the IMF's articles of agreement is required in order for the amendment to take effect.[19]

The IMF reforms would essentially: (1) increase the size of the U.S. quota while commensurately decrease the U.S. share in the NAB by an equivalent amount of approximately $63 billion; and (2) accept the changes in the IMF Executive Board while preserving the U.S. seat as well as its veto power on the board.[20] Despite the public urging of the IMF's leadership to act on the proposed reforms by December 2014,[21] and the open expression by certain IMF members

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14 *Id.* at 2.

15 *Getting Around Uncle Sam*, ECONOMIST (Jan. 31, 2015), http://www.economist.com/news/finance-and-economics/21641260-how-reform-imf-without-congresss-help-getting-around-uncle-sam.

16 Press Release No. 10/477, Int'l Monetary Fund, [IMF], IMF Board of Governors Approve Major Quota and Governance Reforms (Dec. 16, 2010), *available at* https://www.imf.org/external/np/sec/pr/2010/pr10477.htm. The IMF press release specifically recognized the importance of the BRICs by stating, "The 10 Fund members with the largest voting share will consist of the United States, Japan, plus the so-called "BRICs" (Brazil, China, India, the Russian Federation), and the four largest European countries (France, Germany, Italy, the United Kingdom). *Id.* The major realignment in the ranking of quota shares under this reform will result in a Fund that better reflects global realities." *Id.*

17 Truman, *supra* note 13, at 3-4.

18 *Id.* at 4.

19 *Id.*

20 Justification for Appropriations, FY 2014 Budget Request, U.S. Treasury Int'l Programs, at 45, *available at* http://www.treasury.gov/about/budget-performance/Documents/FY2014_Treasury_International_Programs.pdf.

21 Anna Yukhananov, *U.S. Closes Out Year Without Passing IMF Reforms*, REUTERS (Dec. 10, 2014), http://www.reuters.com/article/2014/12/11/us-usa-congress-imf-idUSKBN0JO1UC20141211.

of their continuing disappointment at the U.S. Congress's failure to act,[22] the United States Congress took no action for over five years.[23]

In fact, there has already been a movement to bypass the United States on these measures. On January 28, 2015, the IMF urged its membership to agree on reform measures by June 2015.[24]

> In theory, the IMF could sidestep Congress by leaving America out of the capital-raising. But that would need to be approved by 85% of shareholders, and America has 16.75% of the votes. One reason [the U.S. Congress] might vote against [it] is that its shareholding would drop below 15%, costing it its veto. . .That leaves a more modest option: allowing emerging markets' quotas to increase by enough to give them more say but not by so much as to reduce America's share below 15%.[25]

Critics of the U.S. intransigence in passing these IMF reforms have noted that the failure to reform the institution may weaken it in the long-run, and make it less relevant or powerful as an institution.[26] Further, the diminished power of the IMF, over time, may weaken multilateral approaches to global financial crises, and may give rise to regionalism, bilateralism and other means of dealing with global markets and their disruptions.[27]

On December 18, 2015, President Obama was finally able to sign the IMF reforms into effect as part of an omnibus spending bill.[28] The United States will retain 16.5% of its voting power at the IMF.[29] Nevertheless, further work needs to be done in order to augment an IMF member's voting share as its relative economic strength increases. Moreover, the informal practice of appointing a European to lead the IMF and an American to lead the World Bank may be ended. This may happen as early as July 2016 when the current IMF's managing director, Christine Lagarde, a former French finance minister, ends her term.[30]

Although the U.S. Congress finally acted out of the realization that its inaction was undermining the United States' position and leadership in international monetary policies, its action may be seen as "too little, too late." Efforts to bypass

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22 Ben Blanchard, *China Expresses Regret at U.S. Failure to Pass IMF Reforms*, REUTERS (Dec. 12, 2014), http://www.reuters.com/article/us-china-usa-imf-idUSKBN0JQ0PO20141212.

23 *Getting Around Uncle Sam*, *supra* note 15; *See also* Jonathan Weisman, *Senate Democrats Drop I.M.F. Reforms from Ukraine Aid*, N. Y. TIMES (Mar. 25, 2014), http://www.nytimes.com/2014/03/26/world/europe/senate-democrats-drop-imf-reforms-from-ukraine-aid-package.html; Blanchard, *supra* note 22.

24 *Getting Around Uncle Sam*, *supra* note 15.

25 *Id.*

26 *See generally* The Editorial Board, *Past Time to Reform Bretton Woods*, N. Y. TIMES (May 16, 2015), http://www.nytimes.com/2015/05/17/opinion/sunday/past-time-to-reform-bretton-woods.html.

27 Patrice Hill, *IMF Gives U.S. Congress Year-End Deadline for Passing Reforms*, WASH. TIMES (April 14, 2014), http://www.washingtontimes.com/news/2014/apr/14/imf-gives-us-congress-year-end-deadline-passing-re/.

28 The Editorial Board, *Congress Gets Out of the I.M.F.'s Way*, N.Y. TIMES (Dec. 22, 2015), http://www.nytimes.com/2015/12/22/opinion/congress-gets-out-of-the-imfs-way.html?_r=0.

29 *Id.*

30 *Id.*

the U.S. Congress are already underway. In fact, as the discussion below will illustrate, the train may have already left the station.

III. The Creation of the NDB: Its Organization, Structure, and Mission

In a media note to accompany the informal meeting of the BRICS at the G-20 summit in Brisbane, Australia, in November 15, 2014, it was duly noted that:

> The Leaders also reaffirmed their disappointment and serious concern at the non-implementation of the 2010 IMF reforms, and its impact on the Fund's legitimacy and credibility. Undue delays in ratifying the 2010 agreement are in contradiction with joint commitments by the G20 Leaders since 2009. In the event that the United States fails to ratify the 2010 reforms by the year-end, they called on the G20 to schedule a discussion of the options for next steps that the IMF has committed to present in January 2015. They also emphasized the need to continue the IMF reform processes.[31]

Less than a year later, the Forteleza Declaration was released. On July 15, 2014, at the Sixth BRICS Summit in Forteleza, Brazil, the BRICS formally announced the creation of the NDB and the CRA.[32] The Agreement establishing the NDB was also released on the same date.[33] The five signatories shall have equal voting power.[34] Thus, the NDB is not based on a quota system, at least not at its inception.

The NDB will have a president (an Indian for the first six years), a Board of Governors Chair (a Russian), and Board of Directors Chair (a Brazilian), and will be headquartered in Shanghai, China.[35] The NDB Africa Regional Center will be established in South Africa concurrently with the establishment of the NDB headquarters.[36]

The NDB has initial start-up capital of $50 billion, with each member BRICS country contributing $10 billion. The goal is to reach $100 billion.[37] The NDB is designed to provide loans, loan guarantees, long-term credits and make equity

[31] *See Media Note on the Informal Meeting of BRICS Leaders on the Occasion of the G20 Summit in Brisbane*, BRICS Information Centre (Nov. 15, 2014), http://www.brics.utoronto.ca/docs/141115-brisbane.html.

[32] *See Sixth BRICS Summit Forteleza Declaration*, http://brics6.itamaraty.gov.br/media2/press-releases/214-sixth-brics-summit-fortaleza-declaration.

[33] *See* Agreement on the New Development Bank (July 15, 2014), http://brics6.itamaraty.gov.br/media2/press-releases/219-agreement-on-the-new-development-bank-fortaleza-july-15.

[34] *See* Shannon Tiezzi, *Don't Forget About the New BRICS Bank*, The Diplomat (July 22, 2015), http://thediplomat.com/2015/07/dont-forget-about-the-new-brics-bank/.

[35] Raj M. Desai & James Raymond Vreeland, *What the New Bank of BRICS is All About*, Wash. Post (July 17, 2014), http://www.washingtonpost.com/blogs/monkey-cage/wp/2014/07/17/what-the-new-bank-of-brics-is-all-about/.

[36] Tyler Durden, *BRICS Announce $100 Billion Reserve To Bypass Fed, Developed World Central Banks*, ZeroHedge (July 15, 2014), http://www.zerohedge.com/news/2014-07-15/brics-announce-100-billion-reserve-bypass-fed-developed-world-central-banks.

[37] *See* Agreement on the New Development Bank (July 15, 2014), http://brics6.itamaraty.gov.br/media2/press-releases/219-agreement-on-the-new-development-bank-fortaleza-july-15.

investments in support of funding infrastructure and sustainable development projects in the BRICS countries initially.[38] Financing may then be extended to other low and middle-income countries that will be able to apply for loans in time.[39] The membership of the Bank shall be open to members of the United Nations, and shall be open to both borrowing and non-borrowing members.[40]

The BRICS also announced the creation of the CRA at the same time.[41] Unlike the NDB's pool of paid in capital by its members, the CRA is a pool of $100 billion in available currency swaps to be equally shared by the members in order to provide liquidity to them in the event that balance of payments issues arise.[42] The CRA is funded by China contributing $41 billion, Brazil, Russia and India contributing $18 billion each, and South Africa contributing $5 billion.[43] The agreements establishing the NDB and the CRA will need to be ratified by the legislatures of the respective members before going into effect.[44] A plethora of administrative and operational issues will also need to be addressed and resolved before the two institutions become fully operational.[45]

All five signatory members of the NDB have ratified the agreement establishing it. Russia and China were among the first to ratify the agreement establishing the NDB.[46] Brazil ratified the agreement in June 2015.[47] India and South Africa have also ratified the agreement establishing the NDB.[48] Further, Tito Mboweni, former Governor of the South African Reserve Bank, was appointed as South

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[38] *See* Agreement on the New Development Bank, *supra* note 33, at art. 19; *see also* Alex Blomfield & Ivan Davydov, *A New Development Bank – A New Funding Source and a New Way of Doing Things for Energy and Infrastructure Projects Globally,* King & Spalding (Aug. 4, 2015), http://www.energylawexchange.com/a-new-development-bank-a-new-funding-source-and-a-new-way-of-doing-things-for-energy-and-infrastructure-projects-globally/.

[39] *See* The BRICS Bank, *supra* note 2 (estimating that South Asia alone requires $2.5 trillion in infrastructure investment over the next ten years).

[40] Agreement on the New Development Bank, *supra* note 33.

[41] Treaty for the Establishment of a BRICS Contingent Reserve Arrangement (July 15, 2014), *available at* http://brics6.itamaraty.gov.br/media2/press-releases/220-treaty-for-the-establishment-of-a-brics-contingent-reserve-arrangement-fortaleza-july-15.

[42] *Id.* at art. 1; *see also BRICS Contingent Reserve Arrangement Treaty comes into force*, Russia & India Report (July 30, 2015), http://in.rbth.com/economics/2015/07/30/brics_contingent_reserve_arrangement_treaty_comes_into_force_44497.

[43] *See* Wihtol, *supra* note 8, at 12; *see also* Desai & Vreeland, *supra* note 35.

[44] *See* Agreement on the New Development Bank, *supra* note 33 at art. 49. Art. 49(a) states that, "This Agreement shall enter into force when instruments of acceptance, ratification or approval have been deposited, in accordance with Article 48 by all BRICS countries." *Id.*; Treaty for the Establishment of a BRICS Contingent Reserve Arrangement, *supra* note 41 at art. 22. Art. 22(a) of the CRA states that, "This Treaty shall be subject to acceptance, ratification or approval, according to the respective domestic procedures of the Parties." *Id.*

[45] *See* Wihtol, *supra* note 8, at 12.

[46] *See* Tyler Durden, *De-Dollarization: Russia Ratifies $100 Billion BRICS Bank*, ZeroHedge (Feb. 21, 2015), http://www.zerohedge.com/news/2015-02-21/de-dollarization-russia-ratifies-100-billion-brics-bank; *See also China Ratifies the Freshly-Minted BRICS Bank*, Emerging Equity (July 1, 2015), http://emergingequity.org/2015/07/01/china-ratifies-the-freshly-minted-brics-bank/.

[47] *See Brazil Ratifies BRICS Bank, Currency Fund*, The Bricspost (June 9, 2015, 10:28 AM), http://thebricspost.com/brazil-ratifies-brics-bank-currency-fund/#.ViPiSG7kDz0.

[48] *See South African Parliament Ratifies BRICS New Development Bank Agreement*, BRICS (June 26, 2015), http://en.brics2015.ru/news/20150626/208233.html.

Africa's Non-Executive Director to the Board of the BRICS Bank, while Leslie Maasdorp, who has experience working in senior management at Barclays, Goldman Sachs and Bank of America, was nominated as BRICS Bank Vice President by the South African Cabinet.

Kundapur Vaman ("KV") Kamath, was appointed to be the first President of the NDB on May 11, 2015.[49] Bank operations began in July 2015 at the recently opened Shanghai headquarters of the NDB.[50] The first loan issued by the NDB is expected to be denominated in Chinese renminbi.[51]

It may be useful to make certain important distinctions at this point. At first glance, the function of the NDB mirrors the World Bank's, and the CRA mirrors the IMF's. However, the salient question is whether these new institutions conflict with or complement the established ones?[52] The NDB is not exactly parallel to a number of regionally-focused multilateral banks that fall under the rubric of the World Bank (e.g., the European Bank for Reconstruction and Development, the Inter-American Bank, the Asian Development Bank, and the African Development Bank). The NDB does not have a restricted regional focus since all continents are represented in this new venture and all U.N. member states are eligible to be members of the NDB.

Moreover, this is not the first time that non-Western countries have reacted to the stringent structural adjustment conditionality imposed by the IMF as a precondition to borrowing by its sovereign members. For example, in response to the 1997-98 Asian financial crisis, Asian countries initiated the Chiang Mai Initiative (CMI) in 2000.[53] The CMI was then multilateralized in 2009 to become the Chiang Mai Initiative Multilateralized (CMIM).[54] However, it was never used, even in 2008 during the financial crisis that followed the collapse of Lehman Brothers.[55]

Similarly, the BancoSur (Bank of the South) was established in 2009 by seven Latin American countries in response to IMF conditionality imposed on emer-

49 "Private Banker KV Kamath Named First BRICS Bank Head," Reuters (May 11, 2015), http://in.reuters.com/article/brics-bank-chairman-idINKBN0NW0FI20150511. Kamath successfully assumed his duties in July 3, 2015. *Id.*; *see also* "First BRICS Bank head assumes duty-Indian Foreign Ministry," Infobrics (July 3, 2015), http://infobrics.org/blog/news/2015/07/03/2858/.

50 Allen Cheng, *KV Kamath Brings an Experienced Hand to the New Development Bank*, Institutional Investor (Aug. 23, 2015), http://www.institutionalinvestor.com/article/3482095/banking-and-capital-markets-emerging-markets/kv-kamath-brings-an-experienced-hand-to-new-development-bank.html#.ViPcwG7kDz0.

51 Timophei Borisov, *New Development Bank to issue first loan in Chinese currency*, Russia Beyond the Headlines, (July 29, 2015), http://rbth.com/business/2015/07/29/new_development_bank_to_issue_first_loan_in_chinese_currency_48071.html.

52 *See, e.g.*, Dingding Chen, *3 Reasons the BRICS' New Development Bank Matters*, The Diplomat (July 23, 2014), http://thediplomat.com/2014/07/3-reasons-the-brics-new-development-bank-matters/.

53 *Chiang Mai Initiative: An Asian IMF*, Asian Century Inst. (Mar. 26, 2014), http://asiancentury-institute.com/economy/248-chiang-mai-initiative-an-asian-imf.

54 Hal Hill & Jayant Menon, *Asia's new financial safety net: Is the Chiang Mai Initiative designed not to be used?*, Vox (July 25, 2012), http://www.voxeu.org/article/chiang-mai-initiative-designed-not-be-used.

55 *Id.*; *see also* Desai & Vreeland, *supra* note 35; *see also* Eichengreen, *supra* note 7.

gency loans.[56] BancoSur was designed to provide funding for regional development projects, and each member had one vote. However, BancoSur has a variety of complex problems and is widely regarded to be a failure.[57]

In contrast, Andean nations created the *Corporación Andina de Fomento* (CAF), also known as the "Development Bank of Latin America," in the late 1960's in order to overcome the strict rules imposed by the World Bank on infrastructure loans. The CAF now funds more infrastructure projects in Latin America than the World Bank and the Inter-American Bank combined.[58] Whether the NDB will go the way of BancoSur or CAF remains to be seen.

Nevertheless, it should be noted that all denominations for the NDB and the CRA are made in U.S. dollars.[59] Further, the CRA, Article 14(b)(v) specifically provides that where a member is requesting liquidity support or other precautionary measures, that it be "in compliance with surveillance and provision of information obligations to the IMF."[60] Thus, the linkage to the U.S. dollar and to the IMF, however fragile or temporary, is in the organizational documents.

Further, it is also wise to view the NDB and CRA in a broader policy and institutional context. The BRICS have created a new stock alliance[61] designed to cross list derivatives in order to facilitate the needs of institutional investors who may be interested in the members' stock markets.[62] President Putin introduced the idea of creating an energy association with a fuel reserve bank and an energy policy institute at the sixth BRICS summit where the Forteleza Declaration was made.[63]

Russia has already signed a number of nuclear power cooperation agreements with South American countries, and has entered into negotiations for expanding Russia's natural gas pipelines to China and to India.[64] Thus, Russia is already forging stronger South-South ties in the energy sector, and its proposal to establish a new BRICS energy association may be in furtherance of that policy objective.

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[56] Desai & Vreeland, *supra* note 35.

[57] *Id.; see also* Isabel Ortiz & Oscar Ugarteche, *Bank of the South: Progress and Challenges*, LATIN AM. NETWORK ON DEBT, DEV. & RIGHTS, (2013), http://www.realityofaid.org/wp-content/uploads/2013/02/ROA-SSDC-Special-Report9.pdf.

[58] Desai & Vreeland, *supra* note 35.

[59] *The BRICS Bank, supra* note 2.

[60] Treaty for the Establishment of a BRICS Contingent Reserve Arrangement at art. 14(b)(v), *supra* note 39.

[61] *See BRICS Exchanges Alliances*, MOSCOW EXCHANGE, http://moex.com/s506

[62] *BRICS establish $100bn bank and currency pool to cut out Western dominance*, RT.COM (July 15, 2014), http://rt.com/business/173008-brics-bank-currency-pool/.

[63] *Russia pushes for BRICS energy association*, RT.COM (July 10, 2014), http://rt.com/business/171768-russia-brics-energy-association/; *BRICS plans Energy Association in Wake of New Bank*, WORLD NUCLEAR NEWS (July 21, 2014), http://www.world-nuclear-news.org/np-brics-states-plan-energy-association-in-wake-of-new-bank-21071401.html.

[64] Michael Bastasch, *Putin to Form 'Energy Association' of Major Developing Countries*, DAILY CALLER (July 22, 2014), http://dailycaller.com/2014/07/22/putin-to-form-energy-association-of-major-developing-countries/.

Thus, the mission, objectives, policies, and influence of the BRICS in creating the NDB CRA, and supporting alliances may be far-reaching, indeed. However there is a potentially even more powerful downstream impact of this change to the global financial architecture, as discussed below

IV. Does the NDB Signal the End of the U.S. Dollar as a Reserve Currency?

In revisiting the 1944 Bretton Woods conference, there was a clash of the titans, so to speak, between the U.K. delegate, John Maynard Keynes, and the U.S. delegate, Harry Dexter White, then U.S. Treasury Secretary. The U.K. Government, acting through Keynes, proposed the introduction of a new world currency called the "bancor."[65] The scheme was not accepted, mainly as a result of U.S. reluctance, and the U.S. dollar (tied at the time to the gold standard) became *de facto* the world's reserve currency. Even when the U.S. dollar was delinked from the gold standard in 1971, it remained the world's reserve currency.[66]

The status of the U.S. dollar as a "reserve currency" means, in effect, that it remains in high demand for financial transactions conducted globally by foreign governments and private companies.[67] Thus, the U.S. Federal Reserve is able to print currency to meet this international demand, thus easing the need to use U.S. dollar reserves to pay for imports.

Moreover, the liquidity and size of the international market for U.S. sovereign debt remains high,[68] but this is changing dramatically. In 2004, 90% of the world's reserves were in dollar denominated securities. In 2014, it was down to 60%.[69]

Partly in response to the U.S. dollar moving off the gold standard, the IMF created Special Drawing Rights (SDRs) in 1969.[70] SDRs are composed of a basket of currencies, namely, the U.S. dollar, euro, yen, and English pound. SDRs are allocated to each IMF member based on its percentage of global GDP. SDRs are an interest-bearing instrument that may be freely traded by IMF members.[71]

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65 Alex Newman, *Waking Up to a World Currency,* THE NEW AMERICAN (Sept. 10, 2010), http://www.thenewamerican.com/economy/economics/item/4498-waking-up-to-a-world-currency.

66 *Id.*

67 Liam Halligan, *The Dollar's 70-Year Dominance is Coming to an End,* TELEGRAPH (July 19, 2014), http://www.telegraph.co.uk/finance/comment/liamhalligan/10978178/The-dollars-70-year-dominance-is-coming-to-an-end.html.

68 *Id.*

69 Asad Ismi & Peter Koenig, *De-Dollarization: Is BRICS a Viable Alternative to the U.S. Dominated World Economic System?,* CAN. CTR. POL'Y ALTERNATIVES (Nov. 22, 2014), http://www.globalresearch.ca/is-brics-a-viable-alternative-to-the-u-s-dominated-world-economic-system/5415375.

70 *IMF Factsheet,* IMF (Oct. 3, 2014), http://www.imf.org/external/np/exr/facts/sdr.htm.

71 *Id.*

In fact, when the IMF issued bonds designated in SDRs for the first time in 2009, China bought $50 billion worth.[72] The IMF has also issued SDRs as currency which may be viewed as a "global currency."[73]

On November 30, 2015, the IMF decided to add the Chinese currency, the renminbi, to the IMF's SDR basket of currencies, thereby marking China's transition to having a global currency alongside the U.S. dollar, the Euro, the British pound, and the Japanese yen.[74] The renminbi will officially join the other currencies as the fifth member of the SDR in October 2016.[75] The IMF projects that the weighted currencies in the SDR basket will amount to 8% for the UK pound and the Japanese yen, respectively, 11% for the Chinese renminbi as compared to 31% for the Euro, and 42% for the US Dollar.[76] While China will have to work diligently to make its currency more freely tradable during the remaining months before joining the SDR basket of currencies, the renminbi is widely perceived as replacing the use and the influence of the Euro on financial markets.[77]

This may mean, in effect, that the IMF now views itself as world central bank issuing currency and securities under the direction of the IMF Executive Committee.[78] This practice may harken back to Keynes' original concept of the "bancor" that was designed to herald a new global currency regime.[79]

The idea of monetary unions is not new. Multinational currencies such as the Euro are in common use. Monetary unions are in existence in Central and West Africa (Communauté Financière Africaine or "CFA"). Another monetary union, the "Common Monetary Area," uses the South African Rand in South Africa, Lesotho, Namibia, and Swaziland.[80] The African Union's African Central Bank is scheduled to create a continent-wide currency (called the "afro" for now) within two decades.[81] There is also the Eastern Caribbean Currency Union.[82] Even cyber currencies such as the bitcoin are also in circulation.[83]

There is no reason to believe that the BRICS will not, ultimately, issue their own currencies or securities (e.g., currency reserve bonds and other financial

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[72] Newman, *supra* note 65.

[73] *Id.*

[74] Jeff Sommer, *China Steps Up, but Its Currency Still Has Dues to Pay*, N.Y. Times (Dec. 5, 2015), http://www.nytimes.com/2015/12/06/your-money/china-steps-up-but-its-currency-still-has-dues-to-pay.html; *see also Add Yuan to IMF Currency Basket*, China Daily (Apr. 19, 2011), http://www.china.org.cn/business/2011-04/19/content_22390212.htm.

[75] Sommer, *supra* note 74.

[76] *Id.*

[77] Keith Bradsher, *China's Renminbi Is Approved by I.M.F. as a Main World Currency*, N.Y. Times (Nov. 30, 2015), http://www.nytimes.com/2015/12/01/business/international/china-renminbi-reserve-currency.html.

[78] *Id.*

[79] Alex Newman, *BRICS Regimes Forge New World Bank, Call for Global Currency*, The New American (Apr. 3, 2013), http://www.thenewamerican.com/world-news/africa/item/14983-brics-regimes-forge-new-world-bank-call-for-global-currency.

[80] Newman, *supra* note 65.

[81] *Id.*

[82] *Id.*

[83] *See, e.g., Bitcoin Watch*, available at http://www.bitcoinwatch.com/.

instruments).[84] While the paid in subscriptions are denominated in dollars, the members are not necessarily required to make their transactions using the U.S. dollar. In fact, China has entered into numerous agreements with Brazil, India and Russia that use currency swaps that do not use the U.S. dollar.[85]

Thus, the use of BRICS's currencies separately or in a basket may become an alternative to the use of the U.S. dollar as the reserve currency of choice. The use of South-South currency swaps in lieu of using the U.S. dollar is already well underway, and the viability of this continuing trend has yet to be assessed.

However, the diminishing use of the U.S. dollar as a reserve currency, and the waning influence of the United States that may flow from this, has certain serious long-term foreign policy implications.

Most notably, U.S. anti-corruption laws (e.g., Foreign Corrupt Practices Act of 1977, as amended) and economic sanctions regimes (e.g., in relation to Russia, Syria, North Korea, and Iran) are dependent on imposing penalties and exacting economic costs on the wrongdoer, whether a nation-state, private company, or individual.

The persuasive power stemming from the imposition of severe economic costs in order to force compliance with U.S. laws or sanctions will become increasingly difficult if other nations have alternate currencies and global governance regimes from which to choose. Indeed, many U.S. laws are dependent on the nexus with U.S. banking that use the BIS clearing system (or the Society for Worldwide Interbank Financial Telecommunication (SWIFT)). In sum, it is important to note that that use of U.S. banking systems and dollar denominated currency swaps are an important means of imposing economic and political discipline on errant nations.[86]

Further, it is reasonable to expect that a sanctions regime that is dependent on the use of the U.S. dollar will begin to lose its effectiveness as a foreign policy tool commensurate with the diminished use of the dollar. This may become highly problematic for the United States and its allies in the future, and may change the nature and manner in which the United States conducts its foreign relations.

In fact, "[a]s the renminbi becomes more deeply woven into the global economy, it undermines the ability of the West to impose financial sanctions on countries accused of human rights abuses and other violations, like Sudan and North Korea. Such countries can increasingly carry out transactions in renminbi."[87]

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[84] *BRICS Common Currency Would Help Break Western Financial Hegemony*, BRICS Bus. Mag., (Oct. 22, 2014), http://in.rbth.com/world/2014/10/22/brics_common_currency_would_help_break_western_financial_hegemony_39193.html.

[85] Halligan, *supra* note 67; *see also* Jordan Totten, *BRICS New Development Bank Threatens Hegemony of U.S. Dollar,* Forbes (Dec. 22 2014, 5:00 PM), http://www.forbes.com/sites/realspin/2014/12/22/brics-new-development-bank-threatens-hegemony-of-u-s-dollar/#11acca142945.

[86] *See* Hutton and Wishart, *UK Wants EU to Block Russia from SWIFT Banking Network*, Bloomberg Bus. (Aug. 29, 2014), http://www.bloomberg.com/news/articles/2014-08-29/u-k-wants-eu-to-block-russia-from-swift-banking-network.

[87] Bradsher, *supra* note 77.

V. A River Runs Through It

In conclusion, there may be a cautionary tale here. The above discussion has demonstrated that there is long-standing and deep dissatisfaction with a number of inequities in international governance of global capital markets. This stems from a perceived level of disproportionate recognition[88] and representation on the UN Security Council, the IMF Executive Committee, and other international bodies. Further, there have been decades-long objections even by European nations, most recently by Greece,[89] to the stringent IMF-imposed austerity measures that are preconditions to sovereign borrowing under its rules.

Moreover, there is a growing sense that international economic sanctions are imposed in order to achieve U.S.-led foreign policy objectives.[90]

In creating the NDB and the CRA, the BRICS are establishing an alternate global currency and balance of payments system that is governed in an equal partnership, despite the major differences among the members themselves. Time will reveal whether this is a viable system and a viable alternative to the existing one. However, it does reflect a deeper need to govern and to be governed in a more fair and equitable way. The BRICS have been very clear in expressing their disappointment in the failure to pass reforms to the IMF quota system after more than four years. But what is the true genesis of such discontent?

This river may meander back to a 70-year old debate that was initially won by Harry Dexter White. But perhaps John Maynard Keynes is winning the argument after all. At the Bretton Woods conference in 1944, Keynes suggested forming an International Clearing Union whereby all countries would have accounts denominated in a common currency called the "banco."[91] International accounts would be settled by shifting bancos from one account to another.

Whether the country experienced a deficit or a surplus, the country in question would be required to adjust its exchange rates and pay interest. In other words, even surplus countries would be required to make adjustments, perhaps by liberalizing its imports.[92]

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88 *See, e.g.*, Rumu Sarkar, INTERNATIONAL DEVELOPMENT LAW 5 (Oxford University Press, 2009) (stating, "*Tier I* consists of so-called emerging economies of Central and Eastern Europe . . . and those Latin American . . . and South and East Asian countries . . . that are able to successfully attract FDI and wide-scale FPI . . . .The final test of "graduating" from Tier I is for the subject nation to itself become a bilateral donor") (Emphasis in original).

89 Niki Kitsantonis, *Greeks Go On Strike Over New Austerity Measures*, N.Y. Times (Nov. 27, 2014), http://www.nytimes.com/2014/11/28/world/europe/greeks-go-on-strike-over-new-austerity-measures.html?_r=0.

90 *See* Linda Killian, *U.S.-Germany Tensions Sway EU Sanctions on Russia*, Wall St. J. (Jul. 23, 2014), http://blogs.wsj.com/washwire/2014/07/23/u-s-germany-tensions-sway-eu-sanctions-on-russia/.

91 Nuno Berolsky, An Evaluation of IMF Structural Adjustment Programmes: Lessons for South Africa (Feb. 2000) (unpublished M.S.S. thesis, Rhode Island University), *available at* http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=4&ved=0CCwQFjAD&url=http%3A%2F%2Fcontentpro.seals.ac.za%2Fiii%2Fcpro%2Fapp%3Fid%3D1587414014019082%26itemId%3D1002668%26lang%3Deng%26service%3Dblob%26suite%3Ddef&ei=7L7nVP3gCIm9ggSzgYGQCQ&usg=AFQjCNE_NEXon0Jn9D2FfQlUj8QOdzjNMA.

92 *Id.* at 9.

Harry Dexter White offered a different plan whereby only the debtor nations would have to make adjustments by "putting their houses in order" as a precondition to accessing IMF funding.[93] This is the genesis of the "austerity" measures imposed by the IMF through its structural adjustment programs, and is a precondition to borrowing from its coffers. These austerity measures are felt keenly by all sovereign borrowers from the IMF, most recently by Greece.[94] It is this unequal burden sharing that is borne principally, if not exclusively, by debtor nations that is fueling such discontent.

Whether Keynesian economics should triumph lies outside the scope of this essay, but emerging economies have expressed their clear dissatisfaction with the nature of structural adjustments required to be made by the IMF.

The world economic order instituted through the Bretton Woods conference, combined with the use of the U.S. dollar as the world reserve currency, has ensured U.S. financial dominance over the past 70 years, and has helped bolster its political agendas as well. This system is now being called into serious question by the BRICS in establishing the NDB and CRA.

A Way Forward. It is clear that the world has been shifting from a bipolar world during the Cold War, to a unipolar one after the fall of the Berlin Wall in 1989, to a multipolar one.[95] For example, the G-7 (France, Germany, Italy, the United Kingdom, Japan, the United States, and Canada), became the G-8 (plus Russia) which then became the G-20 (Brazil, China, Saudi Arabia, Republic of Korea, France, Australia, China, Canada, Germany, Indonesia, Argentina, Turkey, India, Russia, South Africa, Mexico, Japan, United Kingdom, United States, and the European Union).[96]

A shift away from the unipolarity of U.S. dominance in world affairs, backed by the strength of its currency, does signal a significant change in the world order. Nevertheless, multipolarity offers new opportunities for engagement, even for the United States. For example, during the December 2009 United Nations Climate Change Conference, President Obama was expecting to meet with Chinese Prime Minister, Wen Jiabao, at the final hours of the conference.[97] Mr. Obama was prepared for a bilateral discussion with China, but was surprised to discover the heads of state from Brazil, India and South Africa also in attendance.[98] In an instant, bilateralism was replaced with multilateralism with an emerging economies block.

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93 Robert Skidelsky, *Keynes, Globalisation and the Bretton Woods Institutions in the Light of Changing Ideas about Markets*, 6 World Eco. 15, 21 (Jan.- Mar. 2005), *available at* http://oxonia.org/WE%20articles/WE_skidelsky.pdf.

94 Amar Toor, *Greek Austerity Measures Linked to Increased Suicides*, The Verge (Feb. 2, 2015), http://www.theverge.com/2015/2/2/7963911/greek-austerity-increased-suicides-financial-crisis-bmj-study.

95 *See, e.g.*, Michael Kakutani, *A Challenge for the U.S.: Sun Rising on the East*, N.Y. Times (May 6, 2008), http://www.nytimes.com/2008/05/06/books/06kaku.html?pagewanted=1&_r=1.

96 Richard Wray, *World leaders relaunch G20 as top economic forum*, The Guardian (Sept. 25 2009), http://www.theguardian.com/world/2009/sep/25/g20-reform-pittsburgh-developing-nations.

97 *The BRICS: The Trillion Dollar Club*, Economist (Apr. 15, 2010), http://www.economist.com/node/15912964.

98 *Id.*

After all, calling for more equitable participation in world affairs by all members of the international community should be welcomed, not feared or vilified. Indeed, more South-South linkages and greater economic integration will act to strengthen, not compromise, the world economy. There is no doubt that the removal of "conditionality" as a means of imposing economic discipline in following the views of Harry Dexter White and others is a daunting prospect. This is especially true if important concerns on the environment, human rights, and other global issues are ignored or subverted. But let us keep in mind that as of the date of this writing, neither the NDB nor the CRA have issued a single loan. Whether IMF-styled "conditionality" will be imposed through NDB or CRA lending, or not, remains an open-ended question at this point.

The BRICS have demonstrated that there are many roads that lead to economic development, and not all of them stem from liberal economics or liberal political theory as a model. This may dismay those who feel and perhaps rightly, that economic development should be concomitant with the respect for human rights, the equitable participation of women in society, and a number of important issues and approaches. Regrettably, this view is clearly not shared by all international actors. Perhaps the BRICS are also implicitly criticizing the linkage of economic discipline with political discipline. The de-coupling of the two may be painful for many, including many policy-makers worldwide, and not simply those located in advanced Western countries.

Navigating a multi-polar world is more difficult when the spheres of influence are less localized in the West and are more widely distributed throughout the globe. Indeed, is it an accident that the IMF and the World Bank are headquartered in Washington, DC while the NDB headquarters is located in Shanghai? There may be those who are secretly thinking that the "bell tolls for thee," United States, but I most emphatically disagree.

Rather than seeing the new ascendancy of multilateralism, particularly as exercised by the BRICS and other emerging economies, as a problem, this should be regarded as an opportunity to widen and diversify U.S. interests with new and dynamic players on the world scene. Although U.S. diplomacy and international relations will become more complex and challenging as a result of acting in a multi-party and multi-dimensional world, it also offers a wealth of opportunities for the United States to work in a newly evolving fabric of interwoven interests, values and ideals.