

Preliminary Study on the Operating Model of the BRICS Development Bank

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March, 2013

The proposal on establishing the BRICS Development Bank is the efforts of years and a major recommendation of the BRICS Forum. Under the organization of the BRICS Forum, experts of all the BRICS countries are conducting in-depth studies on the necessity and feasibility of establishing the BRICS Development Bank. This paper intends as some initial thinking on the establishment of the BRICS Development Bank and its operating model.

I. The operating model of the BRICS Development Bank shall be guided by the market demand.

Under the context of the post-financial crisis, the establishment of a common financial institution not only meets the actual needs of the BRICS countries, but also brings opportunities. The BRICS countries will maintain relatively rapid growth inertia and potential, instead of slowing down development pace like other developed countries in North America and Europe. As an emerging economy, the BRICS are facing pressure from adjustments in exchange rates and imports and exports by conventional developed nations. For instance, the exchange rate dispute between RMB and USD since 2008 serves as the best illustration. It is extremely difficult for a single country to resist such pressure. Only united together, can developing countries strengthen their anti-pressure ability and make their voices better heard, thereby seeking for greater development space. The BRICS countries should work together to promote the reform on international financial institutions, so as to better reflect and meet the current changes and appeals of the world economy. The establishment of a new regional cooperative financial institution within the BRICS will provide large-scale and long-term financing services for large infrastructure projects, promote regional development, channel capital from the private sector, and boost technological and innovation capacities, thereby expediting the development of the BRICS countries.

The current multilateral banks (including the World Bank and the Asian Development Bank) fail to satisfy the financing needs of the BRICS in regional development and a large quantity of infrastructure projects. The main reason is that it is not the main task of the existing multilateral financial institutions to support capital construction, especially large infrastructure development. The World Bank, as the largest development bank in the world, has shifted its work target to poverty alleviation programs mainly in poverty-stricken areas in Latin America and Africa. The Asian Development Bank has a very limited number of BRICS-specific projects, contributing only 8% of the total investment in the BRICS countries. It is unrealistic to expect such multilateral financial institutions to shift their focus to the BRICS to meet the financing needs in the region. The BRICS Development Bank will not be a duplicate of any current regional development bank. It will be committed to designing and constructing an integral part of a new international financial system on the basis of drawing lessons from the recent global financial crisis, striving to become a featured development financial institution, and forming complementary partnership with other international financial institutions to maximize the total benefits.

The establishment of the BRICS Development Bank meets the trend of south-south cooperative development in the new era. In terms of international cooperation and development assistance, the BRICS countries, as developing countries, indicated that they will enhance equal dialogues on the basis of global partnership so as to realize the agreed development objectives of the international community represented by the UN Millennium Development Goals (MDGs), as well as emphasize south-south cooperation among developing countries. The founding of the BRICS Development Bank will not substitute traditional development aids; and the international community will continue to honor its promises to provide aids, assistance in construction, debt relief and technology transfer for developing countries, in particular the least developed countries and regions and people afflicted by disasters and wars. The establishment of an investment mechanism for negotiation and cooperation among BRICS countries will pool more funds and collect more resources to push south-south cooperation. Though economic development shows different features in the BRICS countries, economics of scale constitute a dominant advantage in economic growth. With ample foreign exchange reserves and huge potential of the domestic market, the BRICS countries boast growing purchase power and improving

investment environment, becoming an important pull force in the world economic development. If the edges of these five countries in foreign exchange reserves are integrated and combined to set up a common financial institution, it will promote the establishment of a new international financial order. Under the current global financial system, the establishment of the BRICS Development Bank could help the BRICS countries and other developing countries think in an all-round way, leverage the advantages and avoid the disadvantages and fight for a bigger say. In other words, it will maximize the interests of all the countries on one hand, and promote the sustainable world economic development on the other hand to solve those urgent global issues of our times.

II. The operating model of the BRICS Development Bank shall promote transmission between the government force and the market force.

After weathering through the recent global financial turmoil, most people further realized that “market needs government and vice versa”. In order to get rid of domestic adversities, the governments of many market economies such as the USA began to step into the “front battlefield” of market economy through adjusting government functions. In other words, more emphasis is placed on the role of government as “a visible hand”, in addition to giving play to the “invisible hand” of market. This illustrates that the relationship between the government and the market is dynamically fluctuant, and that the engagement of governments and political factors in economic activities is a natural phenomenon. Hence, as emerging developing countries, the BRICS countries need to, in consideration of realities of developing countries, in particular, actual situations of the BRICS, study the trends of government functional transformation, analyze the characteristics of transmission between the government force and the market force and build a featured development financial institution as a transmission mechanism between the two forces.

In the 21st century, with further expedition of economic globalization, the world economic order will have profound changes, and the world economic pattern will come to face major adjustments. Governments of all the countries are rethinking their roles and positions in the economic development. In spite of varying economic development levels and development environments, the international community has reached a consensus that the government shall perform its significant duty and play an

appropriate role in economic and social development. The BRICS countries are facing two transformation tasks of industrialization and urbanization in the new century, which pose special requirements on the government functions. The first is the function of development strategies planning. The government needs to develop development strategies for industrialization and urbanization, including those relating with population flow and others. The second is the function of market system design and organization. The government, as an essential designer and leader of market system reform, shall fully leverage its own advantage in organization to expedite the construction of market systems. The third is the function of macro-economic control. The government shall exert greater macro-economic control, because the BRICS countries present greater discrepancy between the urban and rural areas and regional disparity. The fourth is the function of social protection. The government shall play a bigger role in ecological protection, narrowing the gap between the rich and the poor, protection of the disadvantaged and provision of public products. The fifth is that the governments of the BRICS countries, as a big force among developing countries, are playing a bigger and bigger role in the intentional arena with increasing influence and corresponding responsibilities. It shall be noted that as the current market systems in the BRICS are not sound and complete and the economic subjects require for incubation and growth, the governments of the BRICS countries, as a market architect and cultivator, should make full use of the advantages in organization and coordination to promote the development of market economy. Hence, the governments shall weaken their presence in microeconomic control and enhance their role in macroeconomic control; accelerate building systems conducive to economic development and create a sound economic environment to pave the way for healthy social and economic development; support the construction of market credit system through leveraging its unique creditworthiness.

It is an important way to speed up the development of the BRICS countries through giving full play to the government's organizational advantage and the role of development financing, integrating resources of the government, the financial industry and enterprises, taking initiatives to build the market, credit system and other systems and promoting transformation with market tools. The government may work closely with development financing, and fully play its role as "a visible hand" to effectively translate the government force into the market force with its organizational

creditworthiness, thereby greatly pushing the national infrastructure development and urbanization pace.

III. Mission, nature and principles of the BRICS Development Bank

1. Mission: Jointly funded by the five BRICS countries, the BRICS Development Bank is founded for the purpose of promoting south-south cooperation. The Bank is intended to provide funds for large infrastructure construction, energy and resources development, energy conservation and emission reduction, environmental protection and other prioritized areas, promote and deepen cooperation among the five countries in economic, development, financial and monetary fields, boost and strengthen the establishment of global partnership among these five countries and promote their sustainable development.

2. Nature: It will be a sub-regional policy bank operating under commercial mode. This development bank will be mainly contributed by government-backed financial institutions, and participated by private capital. Through capital allocation in a market-oriented way, it represents the following features: 1) collective investment, 2) professional management, 3) market management, 4) risk sharing and 5) benefit sharing.

3. Capital scale: The capital scale will be mainly in line with the total GDP of the BRICS countries and in reference to the actual investment need. The capital includes paid-in capital and uncollected capital.

4. Equity distribution principles: Equity distribution shall take into account GDP of the five nations, their foreign exchange reserve, total foreign trade volume and growth rate. The majority of the shares will be controlled by the BRICS governments, while non-BRICS countries and other international financial institutions may also become shareholders. The shares will be mainly held by government-backed financial institutions in the BRICS countries, and private capital will be introduced at the same time. Equity distribution among the BRICS nations shall take into consideration GDP, foreign exchange reserve, total foreign trade volume and growth rate of the countries, which will be calculated with the comprehensive weighted method.

5. Selection of Board Chairman and President: After the location of the head office is settled, Board Chairman shall be selected by shareholders in light of the interests of

the head office's country and other countries. President candidate will be recruited openly on a global scale and engaged on a tenor basis.

IV. Operation management of the BRICS Development Bank

1. Working capital: The initial-stage funds will mainly come from the subscription of shareholders. If the condition permits, it will accept contribution from all sorts of long-term funds and other funds with long-term nature in the shareholders' countries. Money will also be raised through issuing bonds secured by multi-BRICS state credit, funds and direct loans as well as attracting private capital.

2. Business operation: By means of lending, equity investment, syndicated loan, investment by funds, technological assistance and donation, the BRICS Development Bank will provide such financial services as forecast, prediction, information and consultation, as well as long-term financial support for infrastructure projects and R&D and transfer of high-technologies and environmental technologies. It aims to realize the agreed development goals of the international community, especially the UN MDGs concerning poverty alleviation, education, food security, public health and sexual equality.

3. Investment portfolio: 1) donation (about 30% of the total investment) will be mainly used for technological assistance projects such as soft knowledge, technological transfer and capacity building, or initial feasibility studies of lending projects; 2) short- and medium-term loans free of interest (about 70% of the total investment) will be mainly extended to mature SMEs engaged in infrastructure construction, development of high-technologies, renewable energy, environmental and energy saving technologies etc. in the BRICS countries and other developing countries.

4. Operating model: The government of any BRICS country or developing country in want of funds may file a project application to the secretariat of the BRICS Development Bank, which will submit a written project application to the Board of Directors based on evaluation. Once the project is approved, a project contract will be prepared by the Board Secretariat in conjunction with potential project implementer, international institutions, country-specific institutions or the local government, which will be responsible for pushing the establishment and operation of the project.

5. Regulatory and risk prevention systems: Risk guarantee systems and mechanisms should be set up. According to the Basel III Accord, the “tier-one core capital” and “capital conservation buffer” systems should be established, and the risk analysis and pre-warning mechanism shall also be built.

V. Conclusion

The BRICS Development Bank needs to be set up as a common development and financing institution for the purpose of promoting transmission between the government force and the market force, supporting capital construction, energy and resources development, energy conservation and emission reduction, environmental protection and other prioritized fields, thereby boosting sustainable development of the BRICS countries.

In the spirit of cooperation and development, it is well-grounded to believe that the BRICS governments could reach consensus on some issues relating to the specific implementation plan, including the capital scale, capital base and financial structure of the Bank, equity distribution between the BRICS and non-BRICS countries, the determination of cross-border projects, financing methods (securities investment, bond financing and guarantee) and management approaches, the participation and scope of the private sector, the public sector and economic development departments.

Besides the above issues, the BRICS governments may bring up more necessary topics, and the BRICS Forum could prepare more necessary documents on these topics for reference. More detailed information is available from multilateral development banks (the World Bank, the Asian Development Bank, the African Development Bank, the Inter-American Development Bank etc.). These multilateral development banks have rich experiences on most organization and operation requirements for building development banks.

The establishment of the BRICS Development Bank will consolidate cooperation with such international organs as the UN Special Unit for South-South Cooperation (SU/SSC), boost extensive sharing of development experiences and achievements, trading and translation of know-how and technologies among developing countries, develop partnership, and further build a positive international image of BRICS nations as responsible power.