Bank Information Center

INFO BRIEF

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Bank of the South

A look into the new Bank of the South, due to launch in December 2007.

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Eight countries are planning to inaugurate the Bank of the South in December 2007. Joining ALBA countries (Venezuela, Bolivia), Ecuador Argentina, Brazil, Paraguay and Uruguay, Colombia decided two weeks ago that it too would join the initiative. Peru and Chile have so far remained silent.

Technical staff from each country have been intensively negotiating the founding statutes for the Bank of South since April. While some stated benchmarks for reaching key agreements have been missed, the continued progress to build unity behind the ambitious and unprecedented initiative have underscored the significance and complexity of launching the Bank of the South.

A signing ceremony in Caracas is not expected to provide too much more detail. Venezuela has suggested that the first loans will be extended in early 2008. The headquarters will be located in Caracas, with office space donated by Venezuelan workers in the form of the eleventh floor of an existing state owned office building. Regional offices will reportedly be located in La Paz, Bolivia and Buenos Aires, Argentina.

What little information has leaked out about the core agreements and philosophy of the Bank of the South has raised as many new questions as they've answered. For months, negotiating progress on Bank of the South has been slowed somewhat by several central issues. Despite public statements to the contrary, agreements regarding capital requirements,

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member voting structure and institutional functions hinge on the reconciliation of different perspectives for the Bank held by Brazil and Venezuela.

BANK OF THE SOUTH AND THE NEW FINANCIAL ARCHITECTURE

Bank of the South represents the cornerstone to a more wholesale renovation of the regional financial architecture long dependent on Northern banks. A regional monetary fund, a common regional currency, a regional network of state development banks, regional stock and commodities exchanges, a regional Parliament (based in Cochabamba) and a regional Social Fund are only some of the new institutions imagined by the current crop of South American Presidents. Whether these institutions emerge under the auspices of the Union of South American Nations (UNASUR), Bolivarian Alternative for the Americas (ALBA), Community of Andean Nations (CAN) or the Southern Common Market (Mercosur) is unclear.

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New energy cartels are also under discussion, and in some cases forming. Venezuela has pushed for the formation of Petrosur and OPEGASUR was announced by Venezuela and Bolivia, in August of this year but faces a number of significant hurdles. The announcement was been resisted by South America's gas importers (such as Brazil and Chile) under the justification that such a measure would "segregate" gas-producing and gas-consuming countries. Chile, Peru and Brazil have all announced major investments in off-shore Liquid Natural Gas facilities to lessen their dependence on pipeline delivered Natural Gas from their neighbors despite the considerably higher cost of ship-transported LNG. Contrary to the goals of IIRSA- and ALBA- oriented energy integration schemes, the trajectory of national energy policy in South America is toward greater fragmentation.

No Monetary Function

The idea of the Bank of the South emerged as an idea in the first presidential campaign of Hugo Chavez in 1998-1999. As the idea has gained force, Bank of the South has been associated with a mechanism for pooling South America's reserves in order to provide balance of payments support in crisis situations, such as the East Asian meltdown at the time. More importantly, this new monetary fund would diminish the onerous impositions of the IMF in setting harsh conditionality in return for providing a green light for accessing international credit. To be sure, the Bank of the South comes into being at a time when most South American economies have lowered their exposure to IMF influence, with new Stand-By agreements falling to only two in 2007 (Peru and Paraguay). In 2005, 80% of IMF's $81 billion loan portfolio was to Latin America. Today, it's 1% with nearly all its $17 billion in outstanding loans to Turkey and Pakistan.

The total outstanding debt to the IMF in Latin America has fallen dramatically to about $700 million.[1]

Mark Weisbrot, Co-Director CEPR, Rodrigo Cabezas, Venezuelan Finance Minister, and Gustavo Guzman, Bolivian Ambassador to the U.S. in a Oct. 23 Briefing in Washington, D.C. *http://www.cepr.net/content/view/1334/*

This distancing from the IMF been achieved in part on the back of high commodity prices and voracious demand from China and India, which has swelled budget surpluses and lifted the credit ratings of Latin American economies. However, this relative prosperity may also have diminished the urgency to create an alternative monetary fund to replace the IMF.

Brazil has opposed the Bank of the South becoming this alternative lender of last resort. Cabezas indicated in his comments in Washington that the new Bank will not initially offer Balance of Payments loans to its members.[2] Despite an initial Venezuelan proposal favoring budget support, no consensus was possible. The Venezuelan minister promised that a Latin American Monetary Fund is not far behind Bank of the South and is envisioned to play this role, although a medium term budget support function for Bank of the South was not rule out.

Some lessons might be drawn from a similar attempt by Asian nations to pool their reserves as an alternative monetary stabilization instrument to the disastrous IMF advice. The Chiang Mai initiative, established in a 2000 meeting of 10 Asian Finance Ministers created an agreement whereby pairs of nations would lend each other money at favorable terms if help were needed to support an exchange rate during a crisis of capital flight. The ceiling on country-to-country currency swaps for 16 member countries was set at $200 billion, double the $100 billion that South Korea, Thailand and Indonesia had to borrow from the IMF in 1998 in return for implementing harsh reforms. However, even with this self-help arrangement now set at $80 billion, the Chiang Mai initiative could not free itself of IMF supervision. If a country needs to borrow more than 20% of the available swaps, it still has to submit to IMF guidelines on how to run its economy. This conditionality was intended to deter lax economic policies. Initially the currency swap threshold that triggered IMF intervention was only 10%.

Asian countries have built up massive reserves since the 1998 crisis, totaling close to $US 3 trillion. South Korea now has the world's fifth largest reserves at $244 billion, up from almost nothing in 1997. China has amassed $1.2 trillion and Japan has doubled its reserves since 2000 to $888 billion. Yet despite this surplus, which has allowed Indonesia and South Korea to pay off the debts claimed of them by the IMF, the ASEAN

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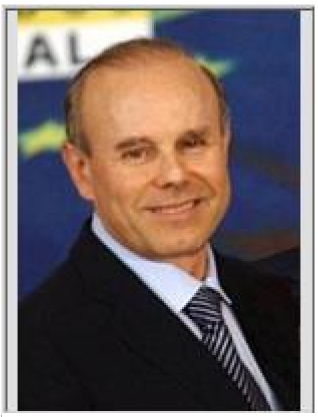
[1] Mark Weisbrot, "Ten Years After: The Lasting Impact of the Asian Financial Crisis," August., 2007, CEPR, *http://www.cepr.net*

[2] Briefing by Venezuela Minister of Finance, Rodrigo Cabezas, Oct. 23, in Washington D.C. hosted by the Center for Economic Policy Research, CEPR. See *http://www.cepr.net/content/view/1334/*

countries do not feel they have the economic surveillance capacity that the Fund has provided. Steps toward the creation of a formal Asian Monetary Fund and a single currency have met with greater skepticism. Although historically opposed by the U.S., the move to establish a formal alternative to IMF oversight is also hampered by Japan and China's battle to establish hegemony over the region. Despite the damage caused by failed Fund oversight and post-crisis advice in 1997-1998, the link between the IMF and the Chiang Mai Initiative remains firmly in place.[3]



Guido Mantega, Brazilian Finance Minister

In addition, the IMF is insinuating itself into the administration of sovereign funds, or the stockpiles of foreign reserves – particularly in the Middle East and Asia. The IMF has recently promoted a code of conduct that opens the door to Fund supervision of the investment practices of sovereign funds.[4] Both the Argentine and Brazilian Directors at the Fund underscored the irony of absent IMF surveillance or advice regarding the sub-prime mortgage market crisis that is unfolding in the U.S. and Europe. Brazilian Finance Minister, **Guido Mantega** noted, "Countries that were references of good governance, or standards and codes for the financial systems, these are the very countries that are facing serious problems of financial fragility putting at risk the prosperity of the world economy." Argentine Minister of Economy and Production added, "The Fund has been so forthcoming in recommended austerity and flexibility that it is embarrassing to see it cannot live up to its own standards." Yet both Ministers call for a "fine-tuning" of the IMF surveillance function and a strengthening of its lending function to more quickly roll out a new liquidity instrument, both of which point to a deepened role for the Fund in addressing future macro-economic volatility rather than a smaller one.[5]

No Conditionality

ALBA members of Bank of the South have been the most vocal in their insistence that Bank of the South be distinguished from the IMF, World Bank and IDB by not conditioning its loans or other forms of cooperation on neoliberal policy reforms. What this claim of unconditional lending actually means is less clear. Minister Cabezas frequently cites the "humiliating penalties" associated with IMF clauses in IFI lending during the 1980s and 1990s that totaled $86 million and over $2.2 billion in debt payments in the "decapitalization" of Venezuela. More generally, many

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[3] Seyoon Kim and Shamin Adam, "Asian Ministers Agree to Partly Pool Foreign Reserves," May 5, Bloomberg;
See also Injoo Sohn, East Asia's Counterweight Strategy: Asian Financial Cooperation and Evolving International Monetary Order," *www.g24.org/sohn0906.pdf.*
4 Ralph Atkins and Mark Schieritz, "IMF joins call for sovereign funds scrutiny" *Financial Times*, Jun 26, 2007.

[5] Statements by Guido Mantega, Minister of Finance, Brazil and Miguel Gustavo Peirano, Minister of Economy and Production, Argentina, Oct. 20, 2007 at the Sixteenth Meeting of the International Monetary and Financial Committee, Washington D.C.

Bank of the South prospective member country Finance and Economy Ministers from Argentina, Brazil, Bolivia, Ecuador and Venezuela at meeting
www.infobae.com/adjuntos/imagenes/98/0169845B.jpg

public and private lenders have historically referenced their own credit decisions on the IMF's blessing, usually in the form of a stand-by agreement in compliance or a clean Article IV report. Conditionality associated with IMF programs often involved slashed public spending, jacked up interest rates, the privatization of state owned businesses and rapid liberalization of capital and commercial markets.

This kind of adjustment lending has declined considerably in Latin America, and IFIs have had to retool their financial instruments to stay in tune with a greater diversity of funding sources. The World Bank has recently reduced interest rates for middle income countries and the IMF, World Bank, and Inter-American Development Bank (IDB) have cancelled several billion dollars in claims made on the most indebted borrowers (Bolivia, Nicaragua, Honduras, Guyana, and Haiti). Policy conditions in the surviving adjustment programs have also been relaxed somewhat.

The Andean Development Bank (CAF) and the Brazilian National Development Bank (BNDES), two of the fastest growing competitors to the Washington-based IFIs, have virtually no policy conditions attached to their loans. The CAF proudly boasts that it imposes no additional demands on the borrower and places its trust in the safeguards and procurement rules of the borrowing country's own national laws. Some have complained that the CAF is not as responsive to borrower needs as it should be. However, this relative absence of red tape is one reason why the CAF has a much shorter project cycle (design to disbursement) and demand for its loans that have nearly doubled over the past 3 years.

The premise of "No Conditionality" also suggest that Bank of the South has or will determine the capacity of its members to borrow and will not place any restrictions on repayment beyond the established terms of the loan.

The World Bank and IDB are also both leaning toward what they similarly refer to as a "country systems" approach. Country systems, according to the World Bank, refers to using a country's own environmental and social safeguard systems (that is, its national, sub-national, or sectoral implementing institutions and applicable laws, regulations, rules and procedures), in cases where they are determined to meet the Bank's standards, in Bank-supported operations. This approach will facilitate a move away from the traditional model in which safeguard and fiduciary policies are applied to only Bank-financed activities toward supporting the development and application of effective policies for all government expenditures. Key to the approach will be an increased emphasis by the Bank on capacity-building and human resource development, which can have a major multiplier effect by leading to broad improvements in the quality of government systems.[6]

The perhaps evident concern with a country systems approach is that national laws or regulations are weak, poorly enforced and set inconsistent standards across countries. How the IFIs determine "equivalency" with current Bank policies is of particular concern. While there may be some benefits from a move toward a country systems approach, NGOs have pointed out that the costs appear to be far higher.[7] For the highest risk investments, a country systems approach greatly enhances a common escape clause employed by the IFIs by allowing them to place blame with governments.

While Brazil has insisted that Bank of the South will not bailout unwise borrowers, it is not entirely clear whether any conditions will be placed on the Bank's loans. The premise of "No Conditionality" also suggest that Bank of the South has or will determine the capacity of its members to borrow and will not place any restrictions on repayment beyond the established terms of the loan. However, the cost structure of Bank of South loans is an area that deserves greater discussion. With a projected $7 billion in initial operating capital and no members with investment grade credit rating, the Bank of the South will not be able to inexpensively or independently access international credit markets.[8] This will drive up the real cost of loans, which Bank of the South may choose to subsidize. Well short of policy reforms, a variety of other lower order conditions involving the scaled cost of loans, the maximum a particular country can borrow,

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[6] See World Bank note on this practice. *http://web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/0,,contentMDK:20266649~menuPK:538163~pagePK:41367~piPK:51533~theSitePK:40941,00.html*

[7] Bruce Jenkins, "Comments on the World Bank's Country Systems Approach," January 27, 2005, Bank Information Center, *http://www.bicusa.org/en/Article.1875.aspx*

[8] By some accounts, Brazil is on track to achieve "investment grade" status no earlier than 2009.

procurement rules, accounting and reporting requirements, etc. have not been clarified.

For the Bank of the South to truly uproot the edifice of IFI hegemony, a priority might be the creation of an alternative source of economic advice and risk assessment that roots out the IFI influence from these last dark corners of development finance gatekeeping.

Perhaps more importantly than any replacement of the emergency funding facility provided by the IMF, is for Latin America to create some competitive option for the signaling function to international markets that the IMF continues to perform. While formal Stand-by agreements are now the exception in the region, some argue that bond buyers and debt holders still look to the IMF to judge the reliability of Latin America's economic health. Whether it's the Paris Club debt renegotiations of Argentina's defaulted debt, or Venezuela's Bonosur bond issues, the IMF continues to influence some of the most prominent financial processes. At the same time, Bolivia's Finance Ministry touts the government's bonafide economic performance by dressing these achievements in the faint praise found in the most recent IMF Article IV reports.[9] Is this genuflection to an institution that has so poorly served the country for the past two decades really necessary? Regional leaders should find this aspect of IMF power as distasteful as previous adjustment reforms. However, in the absence of any alternative regional authority with a similar capacity to qualify the economic risk of investments in Latin America, the IMF will continue to exercise and seek to expand this influence.

Similarly, the World Bank and to a somewhat lesser degree, the IDB, saturate the market of economic ideas with their "sensible advice" via a continuous barrage of analytical work, subsidized scholarship networks and a small army of consultants (12,500 employed at the World Bank alone which makes it the second largest employer in Washington D.C. after the U.S. federal government).[10] With vastly greater research capacities than most governments or universities in Latin America (largely because most research data, despite being financed with IFI debt, remain a private possession of the institutions and not the public good they surely should be), the IFIs continue to skew the agenda for debating economic and social policy in the region.

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Lending Priorities

In a speech in Washington on Oct. 23, Venezuelan Finance Minister, Rodrigo Cabezas indicated that Bank of the South will be guided by three broad lending priorities:

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[9] Press release, Treasury Ministry of Bolivia, August 2007. www.hacienda.gov.bo
[10] Andrew Ward, "Zoellick Urged to Reform the World Bank," *Financial Times*, Oct. 26, 2007

1. Regional Integration
2. Reducing the asymmetries between and within South American countries
3. Provide financing for development

Regional integration is intended to be different than the export-obsessed, foreign investment friendly orientation of IIRSA and FTAA.

Regional integration is intended to be different than the export-obsessed, foreign investment friendly orientation of IIRSA and FTAA. The alternative suggested by proponents of Bank of the South is one that puts national and regional production and South-South investment as a higher priority that the rapid liberalization and insertion of South American economies into the global market. Beyond the recognizable slogans, however, there is little detail.

When asked to provide some examples of possible projects worthy of financing from Bank of the South, Venezuelan Minister Cabezas highlighted infrastructure – both productive (transport, energy) and social (sanitation and education). He cited the proposed oil pipeline between Venezuela and the Andean countries as possible candidate. Cabezas added that large integration projects could possibly involve joint financing from Bank of the South and member state banks such as BNDES in Brazil and BANDES in Venezuela.

In a recent statement, Bolivian Finance Minster, Luís Arce added," we require funding to strengthen *Yacimientos Petrolíferos Fiscales Bolivianos* (YPFB), Bolivia's state-owned hydrocarbons company, mining companies and other strategic initiatives that cannot find concessional financing in the international market."[11] In a recent conference in Washington, Hydrocarbons Minister Carlos Villegas stated that Bolivia plans to double the country's current hydrocarbon distribution capacity (pipelines) and double the production capacity from 40 million cubic meters per day to 80 million within the next five years.[12] In addition to the new investment upon which Bolivia has conditioned revised oil and gas contracts, Bank of the South may be asked to finance new pipelines.

Clearly, Bank of the South would favor lending to state owned companies in partnership with South American state banks. The emphasis on reviving the public sector is consistent with the critique of neoliberal IFIs' emphasis on private sector lending.

However, even in the social sectors, there are expectations the Bank of the South will compensate for the lack of responsiveness by the northern

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[11] Bolivia Treasury Ministry, Press Release, *"El Banco del Sur se fundará la próxima semana con el respaldo de siete Presidentes*," Oct. 23, 2007 *http://www.hacienda.gov.bo/prensa/prensa.php?opt=especi&file=2007-10-23_702.html*
[12] Hydrocarbons Minister, Carlos Villegas, comments at a briefing sponsored by the Center for Economic and Policy Research, Oct. 17, 2007, Washington D.C., *www.cepr.net*.

IFIs. Bolivian Finance Minister Luis Arce reported that his government has had difficulties with the IDB in processing emergency loans to address flooding in February and the problems were more than just bureaucratic. "We are pleased with this achievement that marks a historic moment in international finance. We look on with hope at the formation of a bank that fits within the framework and philosophy of Latin American countries, and will satisfy the demand for lending in the region, and especially for Bolivia that after receiving debt cancellation has found the doors closed regarding additional concessional finance."[13]

Many questions remain that are pertinent to how the Bank of the South's first loans will be distinct from the CAF, BNDES, or even the more common investment loans of the IDB and World Bank:

- What is the range and cost structure of lending instruments offered by the Bank?
- Will Bank of the South lend to non-sovereign entities, such as sub-national governments, or private sector entities?
- What model of integration (IIRSA?) will guide Bank of the South projects?
- How will a Bank of the South financed IIRSA highway be different from a CAF or IDB financed IIRSA highway?
- How will civil society participate in the decision-making process of project selection, design, implementation and evaluation that distinguishes Bank of the South from other IFIs?
- How would Bank of the South projects go beyond social investment and cash transfers to attack the social and economic asymmetries within and between South American countries?
- How would the promotion of integration projects, particularly in the energy sector, surmount IIRSA's failure to diminish the growing asymmetries and tensions between member states?
- How will Bank of the South uphold the highest, if not higher, social and environmental standards in terms of safeguard policies that have been established at some IFIs?

Membership Structure and Capital Commitments

A target of $7 billion in starting capital has been reiterated frequently in the run up to the Bank of the South inauguration. However, a persistent bottleneck in the negotiations on Bank statutes has been over the criteria for capital quotas and the relationship between these quotas and voting rights. An early proposal for capital contributions was for each member to put in 10% of its respective international reserves.

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[13] Bolivia Treasury Ministry, Press Release, "El Banco del Sur se fundará la próxima semana con el respaldo de siete Presidentes," Oct. 23, 2007 *http://www.hacienda.gov.bo/prensa/prensa.php?opt=especi&file=2007-10-23_702.html*

Bank of the South proponents demanded that another significant distinction with Northern dominated IFIs be equal voting power among members. Each member country would have one vote on the Board.

At the same time, Bank of the South proponents demanded that another significant distinction with Northern dominated IFIs be equal voting power among members. Each member country would have one vote on the Board. Current voting structure in the IMF, World Bank and IDB, where votes are awarded in proportion to states' financial contributions, and strongly favor the U.S. and European non-borrowing members. The U.S. controls 30% of IDB Board vote share and about 17% of World Bank and IMF vote shares. By comparison, the eight countries forming the Bank of the South control less than 4% of IMF Board votes, less than 6% at the World Bank and 33% at the IDB. Critics point to de facto Northern control over the IFIs, as illustrated in the recent selection processes that yielded Robert Zoellick of the U.S. as President of the World Bank, Luis Alberto Moreno, the former Colombian ambassador to the U.S. and strongly supported by the U.S., as IDB President, and France's Dominique Strauss-Kahn as the Managing Director of the IMF.

As the region's largest economy, Brazil has reportedly resisted the linkage of equal voting rights with unequal capital contributions, tabling instead a proposal favoring equal capital contributions tied to equal voting rights. A more recent proposal by Ecuador emphasized the criteria that member capital contributions should be no less that the respective contributions each country has in the IMF, World Bank or IDB. In recent weeks, Venezuela has offered its own three-point proposal for capital contributions – that they be proportional to the countries' relative share of the regional economy or regional population; that the contribution be voluntary; and that the contribution be no less than that pledged to the IFIs.

Some of the complications with choosing a just quota system that also permits a one-member one-vote governance system are evident in the scenarios explored in Table 1 (below). We see first that the proposal for allocation of 10% of international reserves just for the 8 original members would not only have Brazil allocating far more than smaller economies such as Bolivia or Ecuador ($16 billion versus $400 million), but also that the total funding would be at least 10 times higher than the $7 billion figure that is often mentioned (See Column 1).

Brazil's foreign reserves have skyrocketed in recent years, almost doubling to $160 billion. With the strong exports driven by high commodity prices together with still-high interest rates and a booming stock exchange, Brazil is seeing a dramatic increase in capital flows that is taking the US dollar from four reais (R$) in 2002 to R$1.75 today, and the Central Bank is rapidly accumulating reserves. While Brazil is in a strong position to use those reserves to back a regional financial institution, the country has little incentive to agree to a percentage set aside with other economies that are not in as strong a position.

If 10% of reserves were to be designated as callable capital, then the $275 billion (the sum of 8 Bank of the South member country reserves) would immediately place Bank of the South above the IDB in terms of perceived credit worthiness. IDB paid-in capital by its 46 member countries is about $4.3 billion, or 4% of the $96.5 billion in callable capital that allows it to issue international bonds to finance operations. Similarly, for the World Bank, Latin American paid-in capital is about 6% of callable capital from the region. The proposal to use 10% of foreign reserves could refer to callable, as opposed to paid-in, capital for the Bank of the South. Venezuelan President Hugo Chavez has suggested that if simply the $200 billion in Latin American reserves invested outside of the region could be transferred back to the Bank of the South or a regional monetary fund, the institution would overnight become one of the largest in the world.

However, few, if any, of these countries have actually passed legislation allowing them to use international reserves for a regional development bank or monetary fund. Bolivia, for example, has studied proposals to allow for the use of the interest earned on its reserves (about $100 million per year), but nothing more. In short, the 10% of member country reserves does not initially seem to be in line with the $7 billion start up capital figure.

A second criterion was that member quotas be no less than current quotas to the World Bank, IMF and IDB. It is not clear if this refers to contributions to a single institution or combined. If we compare contributions to each IFI separately, we see a somewhat opposite result than that for total paid-in contributions to the IFIs by the eight Bank of the South countries. Paid-in contributions to the IMF, World Bank and IDB total about $1.94 billion, $627 million and $1.5 billion, respectively (Columns 2, 3 & 4). Even if combined ($4.1 billion), IFI contributions would set a low floor for capitalizing the Bank of the South, although the disparity between Brazil and the smallest economies diminishes.

Finally, Table 1 explores what the relatives shares would be if they were based on the relative share of each country's population or economy to the larger whole. It is not yet clear what the denominator is for estimating this proportional weight (all 14 countries in South America or only the sum of the eight member countries). Columns 4 & 6 estimate the country's population and GDP as a percentage of the eight-country total of original Bank members and then multiplies that ratio by $7 billion (assumed total start up capital). Columns 5 & 7 take country population and GDP as a percentage of the South American total and multiplies that ratio by $7 billion.[14] The results show that Brazil would allocate well over half of all

[14] Because not all 14 South American countries are likely to be members of Bank of the South, the totals do not add to 100% or $7 billion.

initial contributions in each scenario and be making contributions as much as 120 times greater than the smallest member.

If purchasing power parity estimates of GDP are used, Brazil's share drops only slightly, while the Argentine share goes up significantly. The Andean country shares, particularly Venezuela's, drop.

In Figure 1, the ratio of $7 billion in total startup capital is shown based on single factor distributions. For nearly every variable except current IFI contributions, Brazil's share would be 4 to 20 times higher than most other Bank of the South members. It is therefore probable that member quotas will be set using multiple factors to limit the exposure of Brazil.

Table. 1. Bank of the South Capital Contributions Scenarios

					1		2.0		3		4	
	Pop. million	2006 GDP $US billion)	2006 PPP GDP	Reserves $US billion)	10% of Reserves $US billion)	IMF Million SDR Holdings	IMF Capital Contribu-tions $US million	IMF Vote share %	WB Capital Contribu-tions $US million	WB Vote Share %	IDB Paid-In Capital $US million	IDB Vote Share %
Brazil	188.7	1,100	1,708	163	16.3	359	563.6	1.40	245.5	2.1	465.1	10.75
Argentina	39.1	214	618	43.2	4.32	320	502.4	0.97	132.2	1.1	465.1	10.75
Colombia	45.6	136	363	20.5	2.05	114	179.0	0.39	45.2	0.4	127.7	2.95
Venezuela	27	182	203	35	3.5	317	497.7	1.20	150.8	1.3	249.3	5.76
Ecuador	13.4	41	62	3.5	0.35	33	51.8	0.14	18.2	0.2	24.9	0.60
Uruguay	3.3	19	38	3.5	0.35	50	78.5	0.15	18.6	0.2	49.9	1.15
Paraguay	6	9	30	1.5	0.15	14	22.0	0.05	6.6	0.1	18.7	0.43
Bolivia	9.3	11	28	4.4	0.44	27	42.4	0.08	10.8	0.1	37.3	0.87
8 Country Total	**332.4**	**1712**	**3050**	**274.6**	**27.46**	**1234**	**1937.4**	**4.38**	**627.9**	**5.5**	**1,438**	**33.3**
South America	**372**	**2100**	**3453**	**320**	**32**							
United States	299	13,200	13,201	69,181	6918.1	4,899	7691.4	17.10	1998	16.4	1303	30

	5	6	7	8	5	6	7	8			9	10
	Quota as Relative share of 8 Ctry pop %	Quota as relative share of S Am Pop %	Quota as relative share of 8 Ctry economy %	Quota as relative share of S Am economy %	Quota as Relative share of 8 Ctry pop ($US million)	Quota as relative share of LAC Pop ($US million)	Quota as relative share of 8 Ctry economy ($US million)	Quota as relative share of LAC economy ($US million)	Quota as relative share of 8 Ctry PPP economy %	Quota as relative share of LAC PPP economy %	Quota as relative share of 8 Ctry PPP economy ($US million)	Quota as relative share of LAC PPP economy ($US million)
Brazil	56.8	50.7	64.3	52.4	3979	3551	4498	3667	56.0	49.5	3920	3462
Argentina	11.8	10.5	12.5	10.2	824	736	875	713	20.3	17.9	1418	1253
Colombia	13.7	12.3	7.9	6.5	961	858	556	453	11.9	10.5	833	736
Venezuela	8.1	7.3	10.6	8.7	569	508	744	607	6.7	5.9	466	412
Ecuador	4.0	3.6	2.4	2.0	283	252	168	137	2.0	1.8	142	126
Uruguay	1.0	0.9	1.1	0.9	70	62	78	63	1.2	1.1	87	77
Paraguay	1.8	1.6	0.5	0.4	127	113	37	30	1.0	0.9	69	61
Bolivia	2.8	2.5	0.6	0.5	196	175	45	45	0.9	0.8	64	57
8 Country Total	**100.0**				**7000**	**6255**	**7000**	**5715**			**7000**	**6183**
South America												
United States												

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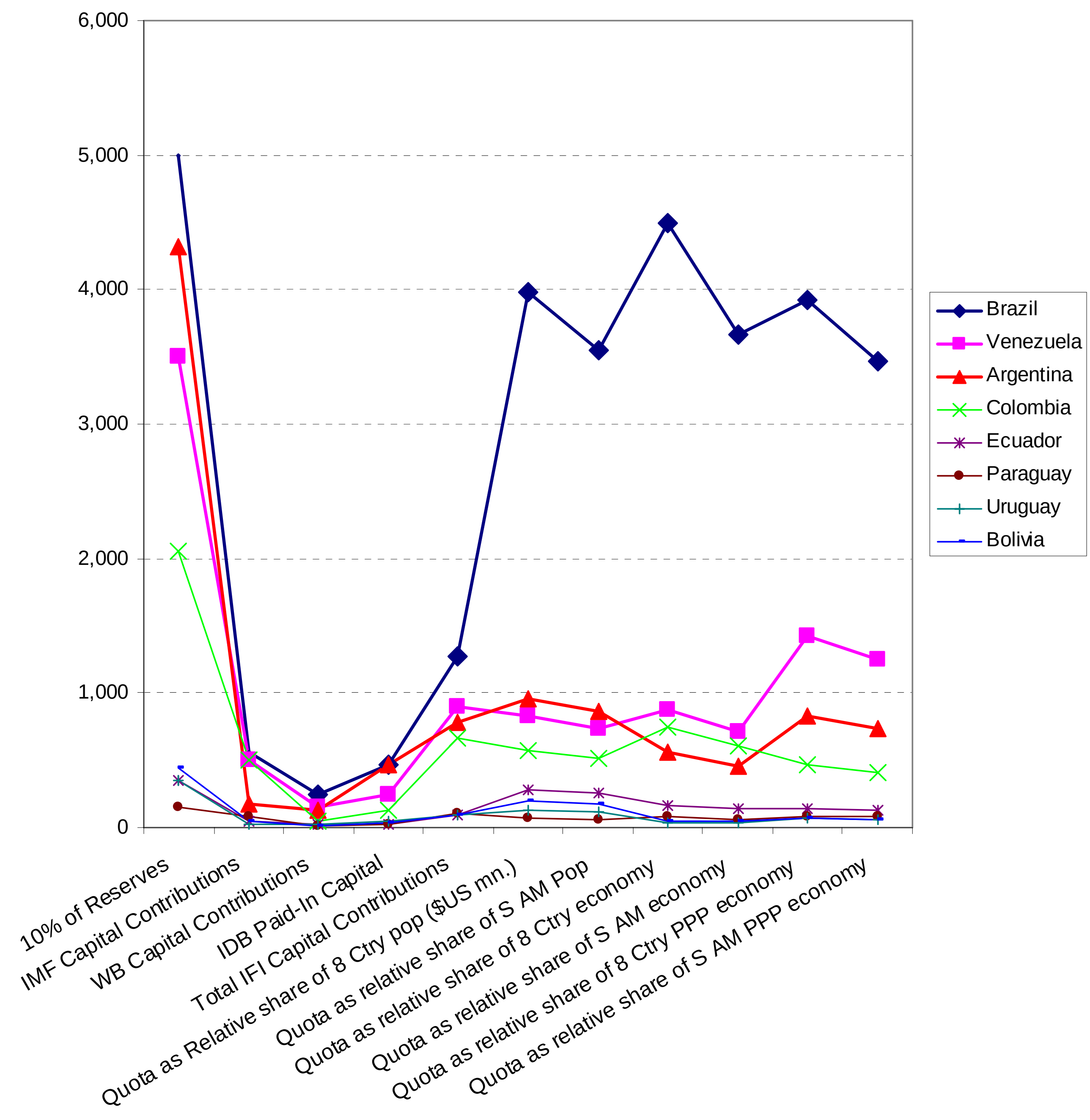
Fig. 1 Bank of the South Capital Contribution Scenarios



Clearly Brazil is not favored by a strict capital contribution formula proportional to the level of international reserves or GDP size. The current debate about reforms to voice and vote structure at the IMF presents an interesting backdrop to the types of issues that are undoubtedly occurring within the technical meetings of the Bank of the South. At the 2006 Fall Meeting of the IMF and World Bank in Singapore, the IMF agreed to "a program to modernize and reform quotas and voice," to be completed before the 2008 Fall meeting. This agreement resulted in immediate ad hoc increases in vote share for China, Korea, Mexico and Turkey and guidelines to negotiate a new quota formula.[15] The Bretton Woods Project points out that the ad hoc vote increases for four countries and a doubling of basic votes (which would not be implemented for years), will decrease the voting weight of advanced economies from 62% of the total to just about 60.5% of the total. African countries would see their vote shares increase a paltry 0.5% to a total of about 6%.[16]

Four variables are weighted in the IMF definition of voting power: 1) GDP, 2) openness of the economy in terms of imports/exports of goods, capital and services; 3) reserves, and 4) variability – which is measured by improvement on average of income and investment. The IMF uses an arcane process of calculating and comparing five different formulas using these contested definitions of concepts (openness) and has clearly not adjusted the weight of impoverished countries, whose loss of power is nevertheless consistent with the massive increase in inequality between the world's rich and poor nations.

According to the Bretton Woods Project, the proposed redesign of any formula that determines voting power is hotly contested, and the last time the members of the Fund tried to reach consensus on a change, the issue became deadlocked. The US preference is for a quota formula based almost entirely on GDP at market exchange rates, which would actually diminish the voting power of most developing countries.

A UK NGO letter to the IMF called for a more far reaching reform based on a double-majority voting system. "*We demand a genuinely democratic structure, which would satisfy the standards of democracy expected at the national level, including the use of population size to help determine voting share. To move towards this goal, we demand the immediate adoption of a double-majority voting system as the first, interim step on the way to comprehensive reform. Decisions by the boards should be made only when both the requisite majority of member governments agree and the*

[15] IMF Issue Brief, "Reform of IMF Quotas and Voice: Responding to Changes in the Global Economy," April 2007. *http://www.imf.org/external/np/exr/ib/2007/041307.pdf*
[16] "IMF Quota Reform is Inadequate, Reaction to IMFC Comuniqué," Sept. 18, 2006, http://www.brettonwoodsproject.org/art.shtml?x=543245

decision garners support of the requisite majority of votes. One-country, one-vote decision-making would counterbalance the one-share, one-vote system. Combining a weighted-voting system with a requirement for agreement by a majority of member governments would move towards ending the inequity in IMF decision making." [17]

Guido Mantega, Brazilian Director for nine Latin American countries advises the IMF against "pseudo-solutions" and calls for "a substantial shift in voting power from developed to developing countries."

Strauss-Kahn has lent some support to this concept in his "campaign" to become the IMF Managing Director. It appears, however, that he is advocating a double-majority consisting of shareholders and "chair-holders" – which is to say a majority of the 24 members of the executive board, a far less dramatic approach that the NGOs' suggestion of a majority of individual country members.

In its statement to the Fund, Guido Mantega, Brazilian Director for nine Latin American countries, proposed greater weight for purchasing power parity (PPP)-GDP in a revised IMF vote formula, a weight reduction for trade openness and variability, and an undefined adjustment factor for smaller, low-income countries. Mantega advises the Fund against "pseudo-solutions" and calls for "a substantial shift in voting power from developed to developing countries." The Argentine Director goes beyond the Brazilian to call for serious consideration of a double-majority voting system that would go farthest in ensuring minimal voting power for the poor.[18]

Brazil has apparently agreed to the one country-one vote rule at the Bank of the South, which appears all the more significant in light of the IMF debate, although initial capital contributions have not been made public. According to one source, Brazil has conceded the fight regarding the voting power of individual country directors and has instead focused on acquiring a greater share of bureaucratic power in terms of the number of administrative posts and negotiating the statutes that dictate the power of the Bank's Presidency. If true, such a strategy would not be much different than that pursued by Brazil in the ongoing realignment at the IDB. The issue of Bank of the South bureaucracy will also be a closely watched dimension of the institution's development.

According to others, Brazil's interests in the Bank of the South are eminently pragmatic. It neither wants Venezuela's energy and cooperation strategies to dominate integration planning, nor does Brazil want to alienate the host of significant private sector investments. Brazil's exports to Venezuela rose by 60% last year. Brazilian multinationals are investing heavily in Venezuela and have ambitious future plans. Odebrecht, a

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[17] UK NGO open statement on governance reform of the IMF, July 21, 2006, *http://www.brettonwoodsproject.org/art-540737*
[18] Mantega, and Peirano op cit.

construction company, has built a new metro line in Caracas and a bridge over the Orinoco, and is building a $2.5 billion hydroelectric dam. Braskem, Odebrecht's petrochemicals arm, has a $3 billion partnership with state-owned Pequiven, which includes building two plants to produce plastic resins. Companhia Vale do Rio Doce is eyeing Venezuela's mineral riches.[19]

REACTIONS TO BANK OF THE SOUTH

Reactions to the Bank of the South have varied within the financial community. Critics have characterized the initiative as an ideological instrument in Chavez's "crusade" against Washington-based multilateral institutions like the World Bank and the Inter-American Development Bank.[20] Others have praised the Bank of the South as a desperately needed Southern-owned alternative to the Northern based IFIs.

Among the Bank's founding members, a surprising range of political views are expressed about the motivations behind Bank of the South. Recent adherents such as Alvaro Uribe of Colombia downplay the opposition to the existing multilaterals. For others, the CAF is included in this "outsider" category reserved for the Northern-based IFIs. "*Regional finance institutions – CAF, FLAR, BLADEX, among others – should be totally evaluated to determine their alignment with the new focus of integration and should it be necessary, to recommend their reconversion toward these ends … the CAF could emancipate itself from the framework of the Washington Consensus and improve the interest rate demanded from its borrowers moreover when these countries are relatively less developed.*"[21]

At least in public references, the targets of Chavez's so-called crusade act unfazed by the new competitor. IDB President Luis Alberto Moreno has publicly downplayed the Bank of South, suggesting that the problems of Latin America are so large that there is plenty of room for more lenders. Recently anointed World Bank President, Robert Zoellick, simply advised the South American leaders to prioritize transparency and avoid corruption.

In a CAF event in Ecuador in late October, its President, Enrique García, felt compelled to argue that the Bank of the South would not affect the solid relationships that the CAF holds with Andean countries. Ecuador, like

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[19] Venezuela and South America: Hugo Chávez moves into banking," *The Economist*, May 10th 2007.

[20] Simon Romero, "Chavez's Plan for a Development Bank Moves Forward," *New York Times*, Oct. 21. 2007.

[21] Amenothep Zambrano, "Un gran banco para una inmensa region del planeta," Casamérica, Sept. 19, 2007, *http://www.casadeamerica.es/es/usuarios/autores/amenothep-zambrano?referer=/es/horizontes/iberoamerica-general*

other Andean nations, borrows over 50% of its multilateral finance from the CAF.

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Privately, however, insiders at the IFIs are beginning to see more immediate financial competition from Bank of the South, but even greater recognition of the symbolic damage the initiative has inflicted on the flagging relevance of their own institutions. The IFIs have all been forced to adapt to stay relevant to their clients.[22] Among other reforms, the World Bank and IDB have retooled their policy (balance of payments) lending by softening some of the requirements as well as the conditionalities. IFI bonds are issued in local currencies to favor Southern exchange rates, and both Banks are exploring transitions to a country systems approach, recent debt cancellation and interest rate reductions for lending to middle income countries can all be seen as gestures to improve the competitive position of the IFI's in the face of growing alternatives for development finance.

Some IDB clients (Peru, Chile, Surinam and Guyana) have so far remained loyal to the IDB, making the recent defection of Colombia, a staunch U.S. ally and rival to neighboring Venezuela, to the Bank of the South all the more remarkable. In a telling statement, Guyanese Minister of Economy Ashni Singh admitted that his country is not prepared to join the Bank of the South. Singh said they would have to explore the implications, not so much in terms of debt ceilings due to recent IFI debt cancellation, but with respect to the political fallout with the country's principal tutor - the IDB. "We are staying abreast of the development with the Bank of the South," stated Singh in a meeting between Guyanese Ministers and IDB functionaries, "Guyana is not closed to the idea of adherence to the Bank of the South, but we are conscious that membership of this financial institution could bring undesirable consequences with respect to the IDB."[23]

BNDES President, Luciano Coutinho, has indicated that in joint partnership with the IDB and IFC, BNDES will create a joint fund to promote infrastructure and productive development in the Brazilian Amazon.[24] The significance of this venture is not only the threat that it represents to the Brazilian Amazon, but the growing recognition by World Bank and IDB managers that they must increasingly seek joint ventures with trusted state banks to avoid being entirely crowded out of the most lucrative private sector project finance markets. The IDB has extended a line of credit to BNDES of over $3 billion in recent years.

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[22] Vince McElhinny, "*Descontento, Confusión, Falta de Transparencia: Cómo ser relevante en América Latina*," July 19, 2007, Bank Information Center. *http://www.bicusa.org/en/Article.3542.aspx*

[23] *Actualidad*, "Guyana descarta convertirse en miembro del Banco del Sur," Nov. 1, 2007, *http://actualidad.terra.es/nacional/articulo/guayana_banco_sur_1979408.htm*

[24] See BICECA, *http://www.biceca.org/es/Article.485.aspx*

Other IFI experts see the Bank of the South as a healthy and much needed antidote to the sclerotic and self-serving culture that seeks to defend institutional survival much more strenuously than actually fulfilling their mandate of eliminating poverty.

Nobel laureate economist Joseph Stiglitz has stated his support for the Bank of the South on a recent visit to Caracas. He said "One of the advantages of having a Bank of the South is that it would reflect the perspectives of those in the South (while in contrast IMF and World Bank conditions) hinder (regional) development effectiveness." [25]

Stiglitz met with Hugo Chavez on his visit and praised his redistributive social policies. He also criticized Washington Consensus neoliberal practices that exploit the regions' people, "undermin(e)....Andean cooperation, and [form] part of the American strategy of divide and conquer, a strategy trying to get as much of the benefits for American companies" at the expense of the region and its people. Stiglitz is one of a small number of external experts being recruited for an advisory committee to the Bank of the South.

ACCOUNTABILITY

Bank of the South proponents have emphasized that this new institution will set higher standards for the democratization of development finance. Civil society has inquired how the Bank will establish a mechanism for greater, permanent civil society input into the Bank's constitution. Questions regarding the design of safeguard policies associated with vulnerable or affected populations, or regarding the environment and transparency have also been raised.

Finance Minister Cabezas responded to such inquiries at an October Washington briefing by stating Venezuela's preference that the Bank statutes include commitments for a social audit mechanism that institutionalizes external oversight and remedy power. However few details were provided beyond principled statements favoring transparency and administrative thrift.

Against the backdrop of the World Bank/IMF annual meetings, civil society representatives happily noted the fact that no credentials were required to speak with Minister Cabezas about Bank of the South and expressed a desire for the continuation of open dialogue. The establishment of a more tangible mechanism for organizing such a dialogue is an urgent task after the December inauguration.

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[25] Rory Carroll, "Stiglitz Endorses Bank of the South," *The Guardian*, Oct. 12, 2007, *http://www.guardian.co.uk/venezuela/story/0,,2189350,00.html*

By most accounts, the establishment of a citizen input or oversight mechanism is a real possibility. More importantly, perhaps, is the identification of the issues that are of highest priority to begin discussing in a more systematic way with civil society. Several areas that stand out are: safeguard and operational policies – transparency commitments being the first and most important; institutional governance and a permanent space for civil society dialogue; and lending priorities regarding how Bank of the South will differ from the IFIs or the CAF and BNDES.