

Will the BRICS Development Bank settle in Shanghai?

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1. Establishing the BRICS Development Bank: Background

On March 28th - 29th, 2012 in New Delhi, India, the 4th summit meeting of BRICS leaders was held. The leaders expressed their views on different issues and proposed the founding of a joint development bank—the BRICS Development Bank—and formally signed a cooperative framework to manage it. The aftermath of the European debt crisis, as well as the uncertainty regarding global economic recovery have affected BRICS nations in different ways. While some show signs of a slowing economy, they must also cope with challenges such as changing models of economic growth, economic restructuring, urbanization, aging societies, etc. In addition, the establishment of a fair, just, inclusive and regulated new international financial order has become a common and urgent demand of emerging economies. The establishment of the BRICS Development Bank is a strong signal that they attempt to change what has once been the territory of the old global powers.

2. Establishing the BRICS Development Bank: Political and Economic Significance

- 1) **More comprehensive cooperation between BRICS countries in fields such as politics, economy, trade and investment:** By jointly establishing a development bank, BRICS leaders have taken a big step towards pushing the “BRICS” from conceptual to substantial cooperation. As an institution of cooperation at the highest level, the bank can help maintaining the economic and financial stability of its member states in the post-crisis age. Although the five countries have different political systems, they still share many geopolitical, economic and trade interests, with some of its members already ranking amongst the world's largest economies. Therefore, setting up a common development bank will further promote the flow of capital between the countries. Each of the BRICS countries has its own advantages and strengths, especially in terms of natural resources. Setting up a development bank has a strong practical significance in terms of their economical, as well as their overall development. It will provide an important guarantee for open investment and trade activities and also promote the reform of the international monetary system. While BRICS countries will be the majority holders, developed countries may be invited to take over minority stakes in the bank. It will fund emerging economies and provide financial support to infrastructure facilities and other development projects. Now that consensus on the BRICS Development Bank has been reached, the most pressing question is the timeframe of its establishment.
- 2) **Formation of a new global economic and political order:** Next to promoting deeper and more comprehensive cooperation between its member states, the

BRICS also give other developing countries a stronger political voice. Economically, the BRICS Development Bank will help to stabilize and expand local currency settlement and loan operations, as well as strengthen important investment projects, financial cooperation, capital market cooperation, and information exchange. There have been discussions about whether the new BRICS bank could be a threat to the dollar's status. While the World Bank has been loaning dollars until now, it could use the BRICS bank as a platform in the future. Therein lies the greatest threat to the hegemonial U.S.-dominated international monetary system. A strengthened political voice of developing countries could lead to the development of a new, “multipolar,” world political and economic order.

2. Why the BRICS Bank should settle in China

First, geopolitical advantages: China, Russia and India are all located in Asia. Whether it is in terms of population or political power, the three countries are in a dominant position, with China's economic and political situation being the most stable. Second, China possesses massive foreign exchange reserves; its total economy ranks second in the world; its trade and investment volume surpasses all other countries. Third, compared to Russia—another permanent member of the UN Security Council—China's political and economic situation is more stable. Finally, China's total bank-scale ranks among the highest in world, demonstrating its strong ability to resist risks. Therefore, we can conclude that China is the best place for building the BRICS bank.

Locating the BRICS bank in China may support the country in taking its place as a new great power in the world; accelerating the process of RMB internationalization; attracting more investment and improving the modern financial system; and stimulating the development of the tourism and exhibition industry.

However, locating the bank in China could also be disadvantageous to the country for a number of reasons. First, the BRICS bank will cause a shock of the current international political and economic system, inevitably affecting the markets of the United States and Europe and perhaps draw a response that influences China's economic development. Second, if the government tries to fight for the BRICS bank settling in China, it will probably have to make significant concessions to the other BRICS members, ending up doing more harm than good. Third, under China's currently imperfect financial market conditions, the structure of the capital market, the monetary system, as well as financial regulations may complicate the accommodation of massive capital in- and outflow. If mishandled, this could become a serious problem.

4. Possible Reactions by the other BRICS Countries and the United States if the BRICS Development Bank would settle in China

Russian scholars point out that Russia's financial market is already freely convertible, whereas China has just opened its market with exchange rates being still under control. Thus, they offered a program that benefits both, giving economic priority to China and monetary priority to the ruble. Chinese scholars, however, believe that with inflation being a serious problem in Russia the ruble cannot be allowed to become the dominant currency. It is easy to see that the two countries disagree on the recognition of the RMB, and that there are still serious differences between the countries. Moreover, considering its own strategic interests in the Asia-Pacific region, the United States is unlikely to support China's bid for headquartering the BRICS bank. History shows that the location of an international institution is likely to cause competition among countries. As a result, neutral countries are more likely candidates for becoming the bank's headquarters. Although not large in size, countries like Switzerland or Belgium, for example, are headquarters of many international organizations. Our discussion led to the conclusion that due to its relative influence and neutrality, South Africa is most likely to become a BRICS bank headquarters. This is because South Africa, Brazil and India have closer ties with the United States, and if the BRICS members agree that one country has one vote, one cannot rule out an alignment of those three countries. In such a case, South Africa is likely to win the bid for headquartering the BRICS Development Bank.

5. Likelihood of the Bank settling in Shanghai

If the BRICS bank were to be settled in China, Beijing would be Shanghai's biggest rival. Beijing has the advantage of being the political and cultural center of China. Furthermore, the headquarters of many major financial institutions are already located in Beijing. Therefore, Beijing's role in cooperation between financial institutions is indispensable.

Nevertheless, Shanghai has many advantages. First of all, Shanghai is already a center of international finance, shipping and trade. Second, as the "first trial" experimental municipality, Shanghai has greater risk tolerance ability and, therefore, a distinct institutional advantage. Due to the uncertainty regarding the BRICS bank, it is more suitable to situate it in a city that is a financial, rather than a political center.

6. Conclusion & Suggestions:

- 1) Founding the BRICS Development Bank has a significant positive effect on promoting regional cooperation, economic growth of developing countries and reducing financial transaction costs among member nations.
- 2) China should strive to become the headquarters of the BRICS bank. At the same time, however, one must consider the possibility of mounting pressure from the United States and the European Union, as well as divergent interests between China and other BRICS nations. The BRICS bank is likely to use a rotating chairmanship system. Therefore, the Chinese government should give more consideration to the members and not the location of the bank's headquarters. In

the end, it is not location but power that decides over who has the final say.

- 3) One has to pay attention to the reaction of the other four nations. A vote will most likely make South Africa headquarter of the BRICS Development Bank.

For the time being, the world economy has overcome the crisis. For international cooperation organizations, including the BRICS Development Bank, the question is how sustainable this situation is. Many international organizations in history have gradually faded from view, such as the Warsaw Pact. Thus, the sustainable development of institutions is a question that requires a more profound discussion.