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South–South Regional Financial Arrangements

Collaboration Towards Resilience

Edited by Diana Barrowclough · Richard Kozul-Wright · William N. Kring · Kevin P. Gallagher

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Preface—About This Book

This book was written in response to calls from both academia and the development community for more information about one of the most interesting and potentially significant new trends in global financial architecture since Bretton Woods. It brings together research from different corners of the globe commissioned by the United Nations Conference on Trade and Development (UNCTAD), in response to a request from its member states for more information about South–South financial and monetary integration—new trends and their potential promise but also limitations. The growth of Southern-led regional financial arrangements (RFAs) has been one of the most interesting and potentially significant trends of recent decades and there was little information about the wide variety of mechanisms being established or their impact. Countries were aware of efforts within their respective regions but not further afield; and policy analysis and advice on regional financial and monetary integration efforts across the Global South was scarce. Working closely with leading international academics, policymakers, and practitioners in the mechanisms themselves, an informal network of experts began sharing research findings at major United Nations intergovernmental meetings and regional commissions and at international academic seminars and workshops, including with experts from Boston University Global Development Policy Center, the University of Geneva, the South African Institute for International Affairs, and the Institute of World Economics and Politics (IWEP) of the Chinese Academy of Social Sciences (CASS). The luxury of long-term research, carried out over several years and building upon prior and ongoing activities by all collaborators in this book, coupled with its global reach, has allowed the network to share increasingly broadly and deeply our data, experiences, and learning, thereby we hope considerably enriching our contribution to the development debate. The fact that it brings together academics and policymakers, sociologists and bankers, and original evidence gleaned from interviews as well as empirical studies, from all parts of the globe, adds further value to the diversity of experiences and views. This book was written before the economic and health shocks of 2020 and 2021 caused by coronavirus, however the lessons it highlights are particularly apt. Some countries were able to benefit from their membership of the RFAs described in these pages; a few could benefit from direct and ad hoc arrangements such as credit swaps; many had few choices; all experienced the kinds of issues relating to short-term and emergency finance covered in this book.

The book aims to present in accessible and readable format discussions relating to different aspects of the financial architecture and parts of the world that are not usually brought together. Because it is written by academics, practitioners, and policymakers, each bringing their different expertise and perspective, it hopes to be a useful source as much for undergraduate and postgraduate courses on political economy, finance, and development, as for the interested lay reader looking to plot a path through debate in the financial and mainstream media. Chapters cover both the broad sweep of monetary history—describing the history of the United States Federal Reserve, the Central Bank of Japan, and the West African Economic and Monetary Union—as well as more granular analysis of the most recent developments, such as Latin America's "virtual" currency the Sucre, alongside the Chiang Mai Initiative, and the rise of Sovereign Wealth Funds. The book also aims to highlight the fact that, while these institutions have (deservedly) garnered a great deal of attention they still need a great deal of support from the international community and cannot be seen in themselves as a final nor perfect answer—we still need a well-functioning and truly universal multilateral solution alongside the rise of regional and partial solutions to a problem and source of vulnerability that—given rising levels of debt and foreign exchange risks—is only likely to increase in the near future.

Geneva, Switzerland — Diana Barrowclough
Geneva, Switzerland — Richard Kozul-Wright
Boston, USA — William N. Kring
Boston, USA — Kevin P. Gallagher

Acknowledgments

This volume acknowledges with gratitude the financial support from the Development Account of the United Nations General Assembly. Papers associated with the project have been presented and discussed at workshops and seminars around the world, including at Boston University's Global Development Policy Centre's Global Economic Governance Initiative; the Freie University of Berlin; the Graduate Institute University of Geneva; the Institute of World Economics and Politics (IWEP) of the Chinese Academy of Social Sciences (CASS); UNCTAD intergovernmental meetings in Geneva as well as a high-level round table at UNCTAD 14 in Nairobi, Kenya; the South African Institute of International Affairs, Johannesburg and a conference hosted by the Union of South American Nations and the Ministry of External Relations and Human Resources, Ecuador. UNCTAD statistican Lyubov Chumakova contributed research findings to the introductory chapter. Jason McSparren provided editorial assistance. Any omissions and faults remain the authors' and editors' own.

Contents

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Abbreviations

ABF1	Asian Bond Fund
ABI	Asian Bond Markets Initiative
ACF	Anti-Crisis Fund of the Eurasian Economic Community
ACM	Eurasian Anti-Crisis Fund
AFC	The Asian Financial Crisis
AfDB	African Development Bank
AIIB	Asian Infrastructure Investment Bank
ALADI	Reciprocal Payments and Credits Agreement
ALBA	Bolivarian Alliance of the Peoples of Our America
ALBA-TCP	Bolivarian Alliance for the Peoples of Our America-Trade Treaty
ALLAC	Latin American Free Trade Association
AMF	African Monetary Fund
AMF	Arab Monetary Fund
AMRO	ASEAN+3 Macroeconomic Research Organization
AMRO	The ASEAN+3 Macroeconomic Research Organization
ARF	Andean Reserve Fund
ArMF	Arab Monetary Fund
ASEAN+3	Association of South East Asian nations plus China, Japan and Republic of Korea

ASP	ASEAN Surveillance Process
Bank Quest Africaine de Devéloppement, BEOA	West African Development Bank
BCB	PTAX of the Central Bank of Brazil
BCEAO	Central Bank for West African States
BCIE	Banco Centroamericano de Integración Económica (CABEI)/Central American Bank for Economic Integration
BCRA	Central Bank of Argentina
BEAC	Banque des États de l'Afrique Centralee/Bank of the Central African States
BIS	Bank for International Settlements
BNDES	Brazil's National Bank for Economic and Social Development
BOP	Balance of Payments
BRICS	Brazil, the Russian Federation, India, China and South Africa
BSAs	Bilateral Swap Agreements
BWIs	Bretton Woods Institutions
CAF	The Development Bank for Latin America
CAF	Corporación Andina de Fomento/(Andean Development Corporation)
CAFM	Council for Financial and Monetary Affairs of ALADI
CARICOM	Caribbean Community
CASS	The Institute of World Economics and Politics (IWEP) of the Chinese Academy of Social Sciences
CDB	China's Development Bank
CEMAC	Central African Economic and Monetary Community
CEMAC	Economic and Monetary Community of Central Africa/Communauté Economique et Monétaire d'Afrique Centrale
CEMLA	The Centro de Estudios Monetarios Latinoamericanos
CIS	Commonwealth of Independent States
CMCP	COMESA Monetary Co-operation Program
CMI	Chiang Mai Initiative
CMIM	Chiang Mai Initiative Multi-lateralization fund
CMIM	Chiang Mai Multilateralization Initiative

CMIM-PL	Precautionary Line
CMU	CARICOM Currency Unit
COMESA	Common Market for Eastern and Southern Africa
CPCR	Agreement on Reciprocal Payments and Credits
CPCR	Reciprocal Payments and Credits Agreement
CPCR—LAIA	Latin American Agreement on Reciprocal Payments and Credits
CRA	Contingent Reserve Arrangement
CSME	Caribbean Community (CARICOM) Single Market and Economy
CSME	CARICOM Single Market and Economy
DBSA	South Africa's Development Bank of Southern Africa
EAC	East African Community
EAMU (planned)	East African Monetary Union
ECA	Economic Cooperation Administration
ECB	European Central Bank
Economic and Monetary Community of Central Africa, CAEMC	Communauté Économique et Monétaire de l'Afrique Centrale CEMAC
ECOWAS	Economic Community of West African States
EDB	Eurasian Development Bank
EMCP	ECOWAS Monetary Co-operation Programme
EMDs	Emerging Market Developing Countries
EMEAP	Executives' Meeting of East Asian and Pacific Central Banks
EMU	Economic and Monetary Union
EMU	Europe's Economic and Monetary Union
EPU	European Payments Union
ERP	European Recovery Programme
ERPD	Economic Review and Policy Dialogue
ESCB	European System of Central Banks
ESM	European Stability Mechanism
ESM	European Stability Mechanism
ESSF	Chile's Economic and Social Stabilization Fund
FCL	Flexible Credit Line
FED	Federal Reserve Bank
FEF	Fondo de Estabilizacion Fiscal
FINPRO	Fund for Productive Industrial Revolution

FLAR	and the Latin American Reserve Fund
FLAR	Latin American Reserve Fund
FOCEM	Fondo para la Convergencia Estructural del Mercosur
FONASUR	Fondo Monetario del Sur
FONPLATA	Fondo Financiero para el Desarrollo de los Países de la Cuenca del Plata FONPLATA
G20	Group of 20 countries
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GFSN	Global Financial Safety Net
IFC	*International Finance Corporation*
IMF	International Monetary Fund
LAIA	The Latin American Integration Association
LICs	Least Industrialized Countries
LTRO	Long-Term Refinancing Operations Programme
MBS	Mortgage-Backed Security
MDGs	Their Millennium Development Goals
MERCOSUR	Common Market of the South/Mercado Común del Sur
MFSC	Monetary Financial Stability Committee
NICs	Newly Industrializing Countries
OCA	Optimum Currency Area
or SUCRE	Unified System for Regional Compensation
PER	CEMAC Programme Economique Regional
PRF	Pension Revenue Fund
RCF	Rapid Credit Facility
REPSS	Regional Payment and Settlement System
RFAs	Regional Financial Arrangements
RFI	Rapid Financing Instrument
RISDP	Regional Integration Strategic Development Programme
RMU	Regional Monetary Unit
RTGS	Real-Time Gross Settlement
SADC	Southern African Development Community
SADCC	Southern African Development Community Conference
SARB	South African Reserve Bank
SBAs	Stand-by Agreements
SCF	Stand-by Credit Facility

SDGs	Sustainable Development Goals
SDRs	Special Drawing Rights
SIP	Regional Interlinked Payment System in Central America (SIP)/Sistema de Interconexión de Pagos
SMEs	Small and Medium-Sized Enterprises
SML	Local Currency Payment System
SQS/NF	Non-Financial Corporations and Quasi-Corporations
SWFs	Sovereign Wealth Funds
TAF	Term Auction Credit Facility
TCI	Taxe communautaire d'intégration
TPSs	Transnational Payment Systems
TRT	Term Repurchase Transaction
TSLF	Term Securities Lending Facility
UDPPP (PG 77)	BOAD Public Private Partnership Development Unit
UMOA	West African Economic and Monetary Union
UNCTAD	United Nations Conference on Trade and Development
URR	An Unremunerated Reserve Requirement
VAT	Value Added Tax
WACB	West African Central Bank
WAEMU	West African Economic and Monetary Union
WAEMU	Economic Community of West African States zone
WAMI	West African Monetary Institute
WAMU	West African Monetary Union
WAMZ	West African Monetary Zone
ZMAO	Zone Monetaire de l'Afrique de l'Ouest

List of Figures

List of Tables

CHAPTER 1

South–South Regional Financial Arrangements in the Twenty-First Century—Promise and Potential

Diana Barrowclough and William N. Kring

As the world comes to grips with the devastating economic and public health consequences of the COVID-19 Coronavirus, Southern-led alternative institutions for finance and development seem more important

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This book brings together research commissioned by the United Nations Conference on Trade and Development (UNCTAD), in response to a request from member states for more information about South–South financial and monetary integration. This has been one of the most interesting and potentially significant

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than ever. This volume charts the dramatic change in the global financial and monetary landscape that has unfolded over the last few decades, in particular, through the expansion of Southern-led and Southern-oriented institutions and mechanisms. The change is profound, and it has moreover not stopped; the evolution of the Southern-led financial architecture is likely to continue, as the South not only adapts to changing global economic conditions, but changes them—increasing its role in global economic governance.

This book takes stock of some of the most interesting adaptations and institutions led by the South with respect to short-term foreign liquidity and emergency finance. It focuses on common currency areas and payment systems designed to avoid exposure to volatile international currencies and to promote a more resilient pattern of interregional trade; the potential for the newly emergent Sovereign Wealth Funds (SWFs) to play a more developmental role; and, the better known short-term liquidity mechanisms that pool foreign exchange reserves or serve as multilateralized swap arrangements that can provide countercyclical finance or liquidity to member countries, oftentimes more quickly and more generously than the International Monetary Fund (IMF). As noted in the preface and below (footnote 1), the book is a response to requests from experts in many countries for more information about these new

trends of recent decades and there was little information about the wide variety of mechanisms being used or their impact. Countries were aware of efforts within their respective regions but not further afield; and policy analysis and advice on regional financial and monetary integration efforts across the Global South was scarce. Working closely with leading international academics, policymakers, and practitioners in the mechanisms themselves, an informal network of experts has been created, sharing research findings at major United Nations intergovernmental meetings and regional commissions and at academic seminars and workshops, including with experts from the Boston University Global Development Policy Center, the University of Geneva, the South African Institute for International Affairs, and the Institute of World Economics and Politics (IWEP) of the Chinese Academy of Social Sciences (CASS). The luxury of this long-time frame and global reach has allowed the network to share increasingly broadly and deeply our data, experiences, and learnings, thereby we hope considerably enriching our contribution to the development debate. This chapter in particular acknowledges with thanks statistical inputs from UNCTAD statistician, Lyubov Chumokova.

initiatives because some have been more successful than others, and many are not well known outside of their immediate borders or regions.

The different experiences described in this volume show that while these Southern-led initiatives offer many and significant benefits to broaden and diversify the global financial architecture, they are only partial and imperfect solutions to the challenges that remain. The institutions that constitute the Southern-led architecture of global financial institutions stand ill-equipped to deal with a truly systemic global crisis—with the added concern that their Northern-led counterparts are just as ill-prepared. Further, many of these new institutions remain untested. That said, they illustrate the promise and underappreciated capacity of Southern-led institutions at the present moment. To fully realize the potential of a Southern-led architecture, further efforts are needed to help these new mechanisms contribute in ways that significantly alter the global financial landscape and the behavior of the institutions within it. Hopefully these alternative institutions can further ignite the evolution of existing institutions to improve lending decisions and expand access to vital resources to contribute to an inclusive and sustainable economic transformation.

1.1 Origins of Alternative, Southern-Led Institutions

The 2007–2008 financial crisis reinvigorated criticism of the global financial order. That said, calls for reform to the global financial architecture for payments and liquidity support were not new and indeed for more than a decade, scholars and practitioners alike had pointed to the increasing frequency and costs of financial crises.

While there is extensive literature on the shortcomings of the current global financial system and Bretton Woods Institutions (BWIs), there are three key factors explored that particularly motivated the Global South in developing and capitalizing alternatives. First, the increasing scale and volatility of capital flows, which was accompanied by an increasing frequency of financial crises over the past decades, led states to self-insure. Through the accumulation of foreign exchange reserves and creation of new multilateral institutions to provide alternative sources of crisis financing and trade support, countries looked beyond the traditional global financial architecture. Second, the IMF misdiagnoses and accompanying procyclical policy prescriptions of the Asian Financial Crisis and the Argentinian Crisis diminished its legitimacy, as the IMF has subsequently acknowledged. Finally, significant changes to the composition of the global economy have yet to be reflected via a rebalancing of the international financial architecture. Reinforcing these three essentially external factors was a more endogenous trend supporting South–South initiatives and South–South trade, as local and regional markets appeared ever more attractive alongside the steady downturn in global trade and stagnating global economy. This section briefly unpacks these motivating factors in order to provide context to the emergence of these Southern-led alternatives.

The first driver of institutional innovation in the South is the increasing economic volatility that has accompanied the deregulation of capital flows on a global scale. As a result, financial crises have become more frequent since the end of the Bretton Woods fixed exchange rate system. Financial crises have occurred more than once per decade since the fall of Bretton Woods (IMF 2017) and the pain of IMF conditionality imposed in return for Fund support has made many countries, especially in Asia, determined to avoid the pain of the past. The credit crunch that followed the 2007–2008 financial crisis, and then the excessive liquidity caused by Quantitative Easing policies in the North, reinforced the gyrations of global capital markets and showed that the current financial architecture was more, and not less, unstable than ever. While some of the institutions explored in this book have roots that predate the 2007–2008 financial crisis, many of the Southern-led efforts represent defensive efforts to deal with the fallout from excessive and volatile capital flows, fluctuating exchange rates, and the dramatic drop in global trade. Further, the 2007–2008 crisis led many countries to redouble efforts to strengthen existing alternative institutions through a variety of means, such as an expansion of institutional capacity and resources.

The second driver of institutional innovation in the Global South was the legacy of IMF missteps in both Latin America and Asia. In the wake of the 2007–2008 financial crisis, as then Managing Director of the IMF Dominique Strauss-Kahn toured Asia, he noted that while the IMF did some things right during the Asian Financial Crisis, it "also did things wrong, and [the IMF has] to accept this." (See for example VOA 2011; and IMF internal evaluation reports, e.g., IMF 2003). While the IMF's

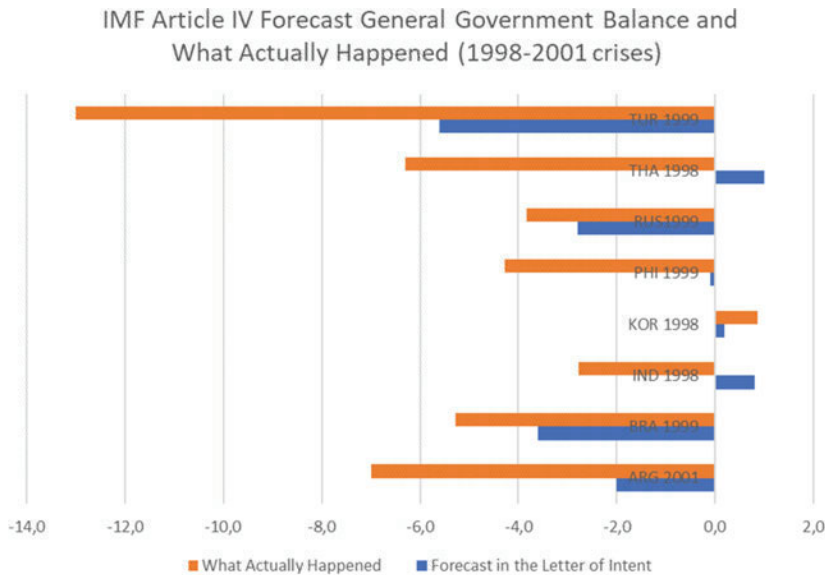

Fig. 1.1 The Disappointment Gap—Crisis the first time around (*Source* UNCTAD, derived from forecasts taken from IMF and country Article IV Letters of Intent; actual data taken from IMF database, year t+1; see UNCTAD 2011:64 for further details)

mea culpa on its past approaches to crises resulted in some subtle shifts,[1] there is considerable evidence that the rhetoric on how its conditionalities have changed is a bit misleading. For example, Kentilikenis et al (2016) identify a fundamental mismatch between the IMF's word on how it has changed and the actual nature of its austerity policies.[2] The policies applied in the wake of the 2007–2008 crisis in practice were still very similar to those used in the previous decade (see UNCTAD 2011: 63–65). Both times, as shown in Figs. 1.1 and 1.2, the actual economic impact of fiscal tightening on Gross Domestic Product (GDP)

[1] Some frequently cited examples include the Fund's acknowledgment of the need for countercyclical fiscal policies in certain types of crises and its rethink on capital controls.

[2] Recent IMF programs in Argentina and Ecuador also follow the same path as taken in the past.