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BRICS INSIGHTS PAPER 6

BRICS IN THEIR REGIONS: EXPLORING THE ROLES OF REGIONAL FINANCE

BY KATHRYN HOCHSTETLER

Introduction

The diversity of sources of international development finance has increased dramatically in recent years. The large emerging powers of BRICS are central contributors to this phenomenon. While they have provided international finance for decades, the quantity and ambition of this finance have seen real advances since 2000. Yet little is known about the details of this lending.[i] This policy insight sets out some of the open empirical questions about the individual BRICS countries' development finance, with special attention to their lending to other countries in their geographic regions.

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[i] Alves AC, 'China's win-win cooperation: unpacking the impact of infrastructure-for-resources deals in Africa', *South African Journal of International Affair,* 20, 2, 2013, pp. 207-208; Bräutigam D, *The Dragon's Gift: The Real Story of China in Africa*. Oxford: Oxford University Press, 2009, pp 19-20; Bräutigam D & KP Gallagher, 'Bartering globalization: China's commodity-backed finance in Africa and Latin America, *Global Policy*, 5, 3, 2014, pp. 346–352; Chin GT, 'The BRICS-led Development Bank: Purpose and politics beyond the G20', *Global Policy*, 5, 3, 2014, pp. 363–373; Hochstetler K, 'The Brazilian National Development Bank goes international: Innovations and limitations of BNDES' internationalization', *Global Policy,* 5, 3, 2014, pp. 360–365; Nyko D, 'Integração Regional, Cooperação Financeira e a Atuação do BNDES na América do Sul no Período Recente', MA thesis, Universidade Estadual de Campinas, Instituto de Economia, 2011, pp. 80-83; Qobo M & D Motsamai, 'Developmental state construction and strategic regionalism: The continental research of South Africa's development institutions', *Global Policy,* 5, 3, 2014, pp. 353–359.

Beyond the current lending patterns, this policy insight also surveys existing theories about regional economic integration, often developed in the context of trade integration, to develop hypotheses about the possible motivations for and consequences of the BRICS countries' regional finance, for themselves and their neighbours. Finally, the focus falls on lending by the national banks of BRICS. While important in and of itself, it also provides hints about how the still-developing collective BRICS New Development Bank (NDB) may set up its operations.

What we need to know: how much, how and why?

Development finance from the BRICS countries often makes newspaper headlines, with splashy announcements of some new loan through the Brazilian National Economic and Social Development Bank for a large hydroelectric dam or Chinese support for a new building for the AU. The gap between public announcements and actual spending can be quite large, however.[ii] Therefore, one of the first questions to be answered is how much money actually passes from the BRICS countries to their neighbours. Answering this question requires paying attention to the full portfolio, trying to capture everyday kinds of finance as well as that which makes headlines. Ideally, research should cover not just contracted loans but also assess how often projects are successfully completed. Preliminary research suggests that the BRICS countries vary in how focused they are on their regions as recipients of their international lending, so it would also be useful to have regional lending placed in context.

Beyond how much money is loaned, how is it loaned? Here, one of the most important questions is whether the loans are made on commercial terms or as concessional finance, or even grants. Another component of the question examines whether conditions are placed on the loans and, if so, the nature of these conditions. Are the loans linked to firms or exports from the BRICS countries? Will they be repaid in natural resources? Are there any policy demands made alongside the loans? These questions are among the most important from the standpoint of loan recipients, as they determine whether BRICS's lending represents a true alternative source of development finance. The World Bank and regional development banks have been dominant actors in the sector for decades. While they have provided critical development assistance, they have used their dominant position to impose numerous conditions on aid recipients, from

[ii] Bräutigam D & KP Gallagher, *op. cit.*; Hochstetler K, *op. cit.*

wholescale economic structural adjustment to environmental and human rights conditions.[iii] Some observers worry about the loss of that policy influence,[iv] while others celebrate the BRICS's lending as potentially more consistent with recipients' development needs.[v]
The answers to these questions will already offer important insights into the reasons the BRICS countries are offering finance to their neighbours. However, it is also important to know to what extent regional finance is the product of a state's overarching foreign policy agenda. If so, is it linked to economic integration processes of trade or infrastructure? Alternatively, is regional finance a 'bottom-up' process, where recipient countries and/or national firms drive the lending patterns? Answers can, of course, include both of these possibilities, with states setting out parameters and quantities that are filled in by bottom-up demands. The next section details what is at stake theoretically in these various alternatives.

Rationales and consequences of regional finance

Why do states, especially those in positions of regional dominance, engage with their regions, even offering development finance? Most answers to this question so far have been developed as explanations of trade initiatives and their consequences, and derive largely from the experiences of industrialised countries. This policy insight also draws on the literature on Latin American economic integration, to suggest how these theories might make sense of the rationales and consequences of South–South finance between the BRICS countries and their neighbours. Two or more of these rationales may be combined as explanations of the lending of particular BRICS countries, although a few of them are incompatible on questions such as the importance of market logics.

Many discussions of regional economic relations begin with the assumption that they are driven by economic rationales that follow market logics (see Mattli for a survey of these).[vi] Potential

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[iii] Anner M & T Caraway, 'International institutions and workers' rights: Between labor standards and market flexibility', *Studies in Comparative International Development*, 45, 2, 2010, pp. 151–69; Wade RH, 'Greening the bank: The struggle over the environment', in Kapur D, Lewis JP & R Webb (eds.), *The World Bank: Its First Half Century*, 2. Washington, DC: Brookings Institution, 1997, pp. 611–736.

[iv] Woods N, 'Whose aid? Whose influence? China, emerging donors, and the silent revolution in development assistance', *International Affairs*, 84, 6, 2008, pp. 1205–1221.

[v] Chaturvedi S, Fues T & E Sideropoulos (eds.), *Development Cooperation and Emerging Powers; New Partners or Old Patterns?* London: Zed Books, 2012.

[vi] Mattli W, 'Explaining regional integration outcomes', *Journal of European Public Policy,* 6, 1, 1999, pp. 1–27.

positive welfare effects of integration come from the ways that regional integration helps to solve economic co-ordination problems and reduce economic and political uncertainties for both private and public actors. Economic integration can, for example, allow firms to take advantage of new economies of scale and develop new comparative advantages. All of the factors of production may become more mobile and better able to pursue new opportunities for production, investment, commerce and labour. Integration may prod governments to harmonise standards and procedures. Public investment in infrastructure can be better co-ordinated so that transportation and communications networks do not end at national boundaries. In the four historical waves of Latin American integration, the third wave of the 1990s was most focused on this set of purposes for integration.[vii] In this view, which represents a kind of null hypothesis about why economic activity takes place, regional finance is simply directed to initiatives that instantiate these logics.

Despite the dominance of market rationales for explaining much intra-regional economic activity, including finance, discussions of BRICS and its development finance often presume these countries have political motivations of one kind or another (for example, Brautigam and Zhang discuss these for China).[viii]

However, while they are all political in the sense of prioritising aims other than (or in addition to) market-based economic efficiency, they vary in terms of the actual aim and whether it is the collective aim of the regional grouping or particular sets of countries within it.

Some of the most common political aims of regional initiatives, including financial ones, are those where the collective group is seeking a hedge against global institutions and/or extra-regional actors. A common understanding of the NDB, for example, is that it is a way of expressing dissatisfaction with the slow pace of change in global economic institutions that include the traditional economic powers.[ix] Regional integration through trade or finance can also

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[vii] Malamud A & GL Gardini, 'Has regionalism peaked? The quagmire and its lessons', *The International Spectator: Italian Journal of International Affairs,* 47, 1, 2012, pp. 116–133; Phillips N, 'Regionalist governance in the new political economy of development: "Relaunching" the Mercosur', *Third World Quarterly,* 22, 4, 2001, pp. 565–583; Riggirozzi P & D Tussie (eds.), 'The rise of post-hegemonic regionalism in Latin America', *The Rise of Post-Hegemonic Regionalism in Latin America*, UN University Series on Regionalism, 4. Netherlands: Springer, 2012, pp. 1–16; Tussie D, 'Latin America: Contrasting motivations for regional projects', *Review of International Studies,* 35, 1, 2009, pp. 169–188.

[viii] Brautigam D & H Zhang, 'Green dreams: Myth and reality in China's agricultural investment in Africa', *Third World Quarterly*, 34, 9, 2013, pp. 1676–1696.

[ix] Chin GT, *op. cit.*

serve as a defensive strategy of building coalitions against other regional groupings or powerful actors.[x] Working together, a group of countries may gain leverage against others, reducing the latter's ability to play them against each other in global negotiations or exchange relations. With the global economic hegemon, the US, in their region, many of the Latin American regional initiatives have had this quality, although the US has also regularly tried to unite the region against extra-hemispheric blocs. The now-moribund Free Trade Agreement of the Americas is the most recent example of this.[xi] These efforts have usually focused on trade, but the financial crises of the 1990s have spurred new efforts to develop regional financial alternatives to global institutions such as the World Bank and the International Monetary Fund, whose rules are both powerful and seen as arrayed against Southern interests.[xii]

Another collective political aim may be to achieve economic development through strategies that are only minimally market oriented. Regional integration may serve several purposes here. For example, it could be aimed at collectively preserving or regaining autonomy over development choices. Participants could be trade and investment partners for each other when market actors are wary, and support each other in the global governance of development options. Within the region, the structure of trade and production might be more favourable to the success of regional firms than global competition would be. Regional integration could even deliberately seek 'solidarity' rather than market-based relations, moving beyond the US-led ideas about liberal market trade and development that have dominated the global economy for decades.[xiii] Latin America's proposed Bank of the South has never quite launched, in part because of disagreements among its major members about whether it should be a simple development bank or reflect a wholly new regional financial infrastructure that was less market-oriented.[xiv]

Another explanation for regionalism sees it as less a collective endeavour than as one organised by and for large regional powers. In his survey of global regionalisms, for example, Katzenstein observes, 'Regions are the creation of political power and purpose. Powerful states tend to

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[x] Tussie D, *op. cit.*

[xi] Malamud A & GL Gardini, *op. cit.*; Phillips N, *op. cit.*; Tussie D, *op. cit.*

[xii] Desai RM & JR Vreeland, 'Global governance in a multipolar world: The case for regional monetary funds', *International Studies Review*, 13, 1, 2011, pp. 109–121.

[xiii] Riggirozzi P & D Tussie, *op. cit.*

[xiv] Rosales A, 'The Banco del Sur and the return to development', *Latin American Perspectives,* 40, 5, 2013, pp. 27–43.

extend their purposes beyond national borders through a combination of strategic action and sheer weight.'[xv] Regional integration behind a hegemon is thought to support that regional power in its global relations and enhance its legitimacy as a representative of the region.[xvi] In addition, the regional power is often assumed to most directly benefit economically and politically from integration, and thus may be willing to pay the costs of integration[xvii] through financial and other offerings.

While it is often assumed that regional powers are behind regionalism, Mansfield and Solingen[xviii] consider that an open empirical question, suggesting further research is needed on when 'regional hegemonies' catalyse and when they present obstacles to regionalism. There is, for example, considerable scepticism in existing work that questions Brazil's willingness and ability to exercise effective leadership or pay the costs of regional integration.[xix] For the BRICS countries, the question of whether their regional lending reflects a hegemonic ambition is perhaps the most important question to be answered.

Conclusion

The growth of development finance from the BRICS countries in the 21st century is a fact. But the implications of that fact depend on knowing a great many more details about how much is being loaned and under what terms, as well as the rationales of the BRICS countries for their lending. The answers to these questions will affect the implications of such finance for the BRICS countries themselves, their neighbours and the entire international financial system. We should not assume that all five BRICS countries are playing similar roles in their regions with their finance. If they are, the collective impact of their lending on the international system is

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[xv] Katzenstein PJ, *A World of Regions: Asia and Europe in the American Imperium*. Ithaca: Cornell University Press, 2005, p. 21.

[xvi] Malamud A, 'A leader without followers? The growing divergence between the regional and global performance of Brazilian foreign policy', *Latin American Politics and Society,* 53, 3, 2011, pp. 1–24; Vieira MA & C Alden, 'India, Brazil, and South Africa (IBSA): South–South cooperation and the paradox of regional leadership', *Global Governance,* 17, 4, 2011, pp. 507–528.

[xvii] Doctor M, 'Prospects for deepening Mercosur integration: Economic asymmetry and institutional deficits', *Review of International Political Economy,* 20, 3, 2013, pp. 515–540.

[xviii] Mansfield ED & E Solingen, 'Regionalism', *Annual Review of Political Science*, 13, 2010, pp. 145–163.

[xix] Burges SW, *Brazilian Foreign Policy after the Cold War*. Gainesville: University of Florida Press, 2 Doctor M, *op. cit*.; Malamud A, *op. cit.*; Riggirozzi P & D Tussie, *op. cit*.

considerably higher, but if they are pursuing quite different visions, then the effects are more localised – felt strongly in their regions, but with less systemic impact.

Patterns in the development finance provided by individual BRICS countries are important in their own right. They gain added weight because BRICS has agreed to form the NDB. The bank was first officially proposed at the BRICS summit in South Africa in 2013 and further developed in Brazil in 2014.[xx] While countries have been assigned initial roles in the NDB, there are still really no details about how it will function. Until the countries agree on those and the NDB begins to operate, the BRICS countries' national lending experiences in their respective regions are one of the best guides about what to expect. The countries' own hopes for and statements about the NDB – and the degree of compatibility among them – provide other hints. Previous South–South financial initiatives such as the Bank of the South were largely stillborn because participant countries had such different visions of development assistance.[xxi] Will the NDB suffer the same problems or will it be the powerful challenger to traditional financial institutions that some expect? The policy insights in this special series provide glimpses of a possible answer.

ABOUT THE AUTHOR

Kathryn Hochstetler, Balsillie School of International Affairs, Canada
Kathryn Hochstetler is CIGI chair of governance in the Americas at the Balsillie School of International Affairs and professor of political science at the University of Waterloo.
hochstet@uwaterloo.ca

[xx] Chin GT, *op. cit*.

[xxi] Rosales A, *op. cit*

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