Chapter 14

BRICS and the International Financial Institutions: Voice and Exit

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14.1 Introduction

This chapter analyses the BRICS' relations with the two international financial institutions (IFIs) with near-universal membership, the International Monetary Fund (IMF) and the World Bank. The chapter, following not just the literature on this topic but also the way actual events unfolded, examines BRICS' "voice", i.e. expressions of discontent with and efforts to reform the IFIs, and creation of pathways to "exit", i.e. the beginnings of BRICS-led financial institutions, specifically the Asian Infrastructure Investment Bank, the New Development Bank, and the Contingent Reserve Arrangement. The chapter argues that explanations that draw in a detailed manner from specific institutional features and policies do a better of job of accounting for both partial successes with voice and what the new institutions mean for the postwar multilateral order. The chapter also charts possibilities for refining future research on this topic.

14.2 BRICS and the International Financial Institutions: Voice and Exit

The relative economic rise of large emerging economies (BRICS) in the last several decades has been one of the most monumental changes in the global economic landscape. For instance, in 1997, the year of the Asian Financial Crisis, the G20 emerging economies' share of world economic output was about 27%; whereas, the same number for the G20 advanced economies was approximately 45 per cent. By 2015, however, these emerging economies had increased their share of world GDP to 40%, as the G20 advanced economies' share declined to about a third. In other words, the importance of the two groups of countries for the world economy had almost reversed in 1997-2015.[1] China, in particular, has seen unprecedented growth levels, making its individual share of world GDP in 2015 over 17%. Meanwhile, in 1997-2015, the USA's share of world GDP declined by 5 percentage points, making the 2015 US GDP slightly smaller than China's. And, once the second largest world economy, Japan's GDP in 2015 was only about 4.5 percent of the world's total economic output.[2] The 2008 financial crisis, which threw the USA into the Great Recession and continues to affect parts of Europe in the form of a debt crisis, has further solidified this seemingly tectonic shift. The shift has also raised numerous questions regarding the governance of the global economy, particularly as it pertains to its key international financial institutions (IFIs) with universal membership, the International Monetary Fund (IMF) and the World Bank (WB). Not only have these institutions come to be seen as representing the economic asymmetries of decades gone by, but the BRICS' enhanced capacity to contribute to the institutions has rendered them more important for institutional functions, such as lending, and thus for governance [Kaya, 2015].

[1] There are valid disagreements regarding the coherence of BRICS as a category (see Kirton [2015] for a review of different perspectives). Nonetheless, BRICS' activities within and related to the IFIs show a relatively high degree of cohesion [e.g., Cooper and Farooq, 2013]. Exploring the origins of this cohesion constitutes a different analysis altogether, but it plausibly emerged as a byproduct of institutional factors in addition to BRICS' coordination. In the IFIs, discussions on formal representation (voting rights and seats on the Executive Board) centre around country classifications, pitting institutionally dominant advanced economies against emerging and developing economies. Hence BRICS face a strong incentive to coalesce around as unified of a position as possible (surely, this does not mean their preferences are perfectly aligned). As discussed here, BRICS have endorsed clear goals: reducing the dominance of advanced economies in a way that carves out more autonomy for their policies and representation [Kaya, 2015].

[2] These numbers were calculated based on GDP, PPP (constant 2011 international USD) from the World Development Indicators. For a skeptical perspective on the rise of BRICS, see Sharma [2012].

This paper assesses the rise of BRICS in the context of IFIs. The recent story of BRICS in the IMF and the World Bank has been one of both "voice"—articulations of dissatisfaction with the IFIs' existing structures and pressing for reform—and creating potential pathways of "exit" from the institutions [Hirschman, 1970].[3] While notions of voice and exit mesh with actual events as well as the way in which observers have studied those events, it is important to note at the onset that at this point exit neither means abandonment of existing institutions, nor creating true substitutes for them. Rather, questions about exit centre around institutional arrangements led by BRICS, which boost the credibility of the threat of exit and could plausibly constitute pathways to exit at a future point.

BRICS have exercised their voice, namely discontent, with two related but distinct aspects of these institutions: 1) the distribution of voting power, thus formal power, within the institutions; 2) policies of key concern to them—specifically controls on the capital account and the expansion of the basket of currencies that make up the Special Drawing Right (SDR), which is a reserve asset and the IMF's unit of account. In both these realms, the BRICS' attempts to alter the institutions more in line with their own preferences has met with some success. At the same time, the credibility of the BRICS' so-called exit from the two IFIs has particularly been enhanced since the creation of the New Development Bank (NDB) and the Contingent Reserve Arrangements (CRA) in 2014 and the launch of the Asian Infrastructure Investment Bank (AIIB) in 2015.

The relevant literature, in turn, has advanced a number of variables in explaining the BRICS' success with voice, including: the pressures created on the IFIs by the BRICS' credible threat of exit; the BRICS' effective

[3] In Albert O. Hirschman's [1970] original conceptualization of "exit" and "voice", customers' abandonment of the firm's products denotes the exit option, whereas in using their voice, the customers appeal to the firm's management to fix their discontent related to the deterioration of the product. Not only did Hirschman explore his framework in the context of organisations and politics, his set-up has been influential within political science [e.g. Drezner, 2007]. As will be shown, it is particularly suited to understanding the theory and empirics of BRICS and the IFIs. Differently from exiting the products of a firm, however, exit from a multilateral institution more likely involves a state's disengagement from the institution, and only rarely formally abandoning membership in the institution.

negotiation strategies, and the particular institutional features of institutions, such as the nature of their funding. Explanations for BRICS' enhancing of "exit" options seem similarly varied: each of the BRICS have domestic rationale for pursuing the NDB and the AIIB; the BRICS, particularly China, could have "counter-hegemonic" desires; and only partial success with voice in exiting institutions propels exit from those very institutions. There, thus, seems to be a complex dynamic between "voice" and "exit". Some see inadequate progress with voice compelling exit from the IMF/WB, while others identify exit as enhancing influence within the institutions. For example, the presence of the AIIB is interpreted as due to the dissatisfaction of the BRICS with the IFIs as well as a reason for BRICS' success with reforms in the IFIs.

Although the literature has adequately spelt out "voice" and "exit" rationales, there is room for teasing out the dynamics between these two. Particularly, even though the threat of exit did not seem more severe in the case of the IMF, the BRICS have nonetheless received more concessions in that institution relative to the World Bank in 2008-2010 [Kaya, 2015]. In other words, the threat of exit does not seem to adequately explain the degree of success through voice. Rather, it seems to be the case that a degree of exit—in this case the creation of the AIIB and the NDB with functions similar to those of the World Bank's—follows lack of adequate success with voice. Further, to more fully explain how BRICS have exercised voice successfully, consulting the IFIs' particular institutional characteristics (such as, exiting rules or autonomy of the staff) as well as the preferences of the dominant powers seems crucial [*ibid.*; Gallagher, 2014].

The presence of voice and the credible threat of exit also raises questions about the durability of the post-war order led by the USA and its allies, including the European Union and Japan. Obviously, since existing institutions reflect the preferences of their creators disproportionately [Ikenberry, 2000], any success BRICS have with reform is, by definition, going to change the institutions away from the dominant states (regardless of whether the dominant powers approved of such change). But, such change could ultimately boost the legitimacy of these institutions, thereby prolonging the post-war order. Indeed, voice aims to reduce the prevalent discontent with the institution, and it is a sign of "loyalty", that is the participant's continued interest in the institution [Hirschman, 1970]. At the same time, some of the successes that BRICS appear to have scored simultaneously bind them to the existing institutions. For instance, the Chinese currency (renminbi)'s inclusion in the IMF's SDR basket is a source of prestige for China, but it was contingent upon China promising further capital account liberalisation in accordance with IMF norms. Yet, if exit begins to dominate voice, then the post-war order, which has already weakened due to factors not related to the BRICS' rise, could further disintegrate. The verdict, however, is out on whether the creation of new institutions truly means exit from existing ones (doubtful) and whether exit will dominate voice (also doubtful).

The rest of the chapter, first, discusses BRICS' partial success with voice, i.e. their efforts to alter existing institutional rules and norms and the extent to which these efforts came to fruition. It then discusses the BRICS' threat of exit with an emphasis on the AIIB, the NDB and the CRA. Each of these sections contains a critical and synthetic assessment of existing explanations. The final section turns to the question of the impact of these developments on the US-led post-war order.

14.3 Voice

The proceeding discussions examines the BRICS' calls for reform (i.e. expressions of discontent) within the IMF and the World Bank along two dimensions: 1) changes to (formal) governance rules and procedures, and 2) policy changes. Surely, governance and policy changes are inextricably related – the former likely spurs the latter, but these categorical distinctions serve analytical clarity, and they also follow the way actual negotiations took place.

Discontent with governance structures

In 2008-2010, members states in both the World Bank and the IMF reformed the distribution of voting power (across the membership), the method of calculating each state's voting power, and the structure of the

Board of Directors [Kaya, 2015, Chapters 5 and 6].[4] Importantly, as a result of these reforms, the rate of change in the G20 emerging economies' total voting power within the IMF and the World Bank were 27.74 per cent and 18.62 per cent, respectively [*ibid.*, p. 173, Table 6.4]. Such a change has meant that the G20 emerging economies as a group ended up with more voting power than G20 European economies [*ibid.*]. Within the IMF, China increased its voting power from under 3 per cent to over 6 per cent, making it the third largest shareholder. India, Russia, and Brazil also got promoted to being among the top ten shareholders in the IMF. Further, the IMF moved to an all-elected Board, removing the privilege of some states to appoint their Directors. While the effects of this reform are yet unclear, it was a move toward flattening institutional hierarchies.

Not just the significance of these reforms, but also the length of time it took US Congress to ratify them—Congress passed the bill endorsing the change, which naturally required an increase in American financial contributions (known as the quota) to the IMF, at the end of 2015—attracted a great deal of attention. The US Congress' recalcitrance was seen as giving impetus to the formation of alternative institutions, particularly the AIIB.

Against this backdrop, the rest of this sub-section focuses on BRICS' efforts to alter the way in which the IMF calculates members' voting power (based on quotas). It also contrasts this success with BRICS' less successful efforts at the WB. This selected focus illuminates the key factors at work and the main issues of debate. Importantly, the benchmark against which to judge BRICS' efforts here are not subjective assessments of how much the BRICS' power should have been boosted, but what the BRICS' pre-reform demands were. In this way, instead of a subjective yardstick that shifts across actors and authors, the analysis can focus on a benchmark that is relatively more objective and consonant with institutional debates.

[4] Other works that discuss select dimensions of these reforms are: Woods [2010]; Wade [2011]; Lesage *et al.* [2013].

Reforming the quota formula in 2008

Quotas in the IMF serve critical functions, as they determine the member states' financial contributions to the institution, thereby their relative voting power. A member's quota can also affect the size of the loans the member receives from the institution. Even though the ultimate distribution of the quotas does not depend solely on quota formulae, by virtue of forming the technical reference point for the quota distribution, quota formulae carry great importance. In 2008, the IMF moved from an opaque system of multiple quota formulae to a single one with some variables of preference to the rising states, though the new quota formula did not reflect all of the rising states' demands.[5]

The BRICS began pushing for a reform of the quota formulae soon after the 1997 Asian Financial Crisis, during which the IMF conditionality imposed on borrowing members, particularly Thailand, S. Korea, and Indonesia, was seen as too austere [e.g., Stiglitz, 2002]. In turn, the IMF's seemingly unfair treatment was seen as intrinsically related to the Western powers' disproportionate influence over the institution [e.g., Birdsall, 2006]. In a 1997 Executive Board meeting, the Chinese Executive Director emphasised that "in order to solve the protracted anomalies in quota calculations and distributions, I would like to stress my support for a Board discussion on quota formulas to take place …" immediately [IMF, 1997, p. 13]. Several years later, the Brazilian Director again expressed a sentiment shared among the large emerging economies [IMF, 2001, p. 6]:

> Preserving the legitimacy of the [IMF] depends on the ability to adapt the quota structure to reflect changes in the world economy… consensus on a new quota formula that can better support these objectives is an essential aspect of the new architecture of the international monetary system, and should be treated by the Board with the corresponding importance and priority.

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[5] For a history of quotas and the various formulae used until 2015, see Kaya [2015, Chapter 3]. For most of the institution's history five formulae and two datasets were used.

A putative turning point came with the 2006 "Singapore Resolution," which committed the IMF to boosting the voting power of countries that had experienced sustained levels of high economic growth and to focus on the voice of low-income countries. Taking an ad hoc step toward this end, in 2006, China, Mexico, South Korea and Turkey got quota, thus voting power, boosts.

The structural change, however, came two years later with the introduction of the 2008 quota formula, which Table 1 summarises. Along the BRICS' preferences, the weight of the GDP in this new formula was significantly larger than in previous formulae, permitting the fast growing economies to translate some of that economic capacity to representation within the IMF. The inclusion of GDP calculated at Purchasing Power Parity (PPP) exchange rates, boosted the large emerging economies' economic size and therefore relative voting power. This shift was a first for the institution, since up to that point, only GDP calculated at market exchange rates had been a part of the formula. And, it met BRICS' long-standing demands. For instance, in the 2002 discussions on the issue, the Indian representative put it unequivocally: "Quotas and hence contribution to Fund resources should be on the GNP/GDP computed on a PPP basis" because, as opposed to GDP converted at market exchange rates, GDP PPP "better reflect the real value of total output produced by a country" [IMF, 2002, 3, 6]. In the discussions leading up to the formula, the Chinese central bank's Deputy Governor echoed these views, "we believe a quota formula including PPP GDP, which is simpler and more transparent, is the most effective way to raise the overall share of developing members" [Xiaoling, 2007].

Further, given the build-up of their reserves, the retention of reserves in the 2008 formula revision was a boon to boosting the BRICS' quota and thus relative voting power. Reserves had all along been a factor in the IMF's quota calculations, but its retention in the formula was nonetheless subjected to intensive debate pre-reform. If quotas are seen as a benchmark for accessing loans from the IMF, then the higher reserves of a country, the lower its need for such funds. A number of advanced economies initially took this view, but the final outcome was in accordance with BRICS' desire to retain reserves.

Table 1: IMF's Quota Formula

CQS = $(0.5Y + 0.3O + 0.15V + 0.05R)^k$ CQS = calculated quota share Y = a blend of GDP converted at market rates (60 percent) and PPP exchange rates (40 percent) averaged over a three-year period. O = the annual average of the sum of current payments and current receipts (goods, services, income, and transfers) for a five-year period V = variability of current receipts and net capital flows (measured as a standard deviation from the centred three-year trend over a thirteen-year period) R = twelve-month average over a year of official reserves (foreign exchange, SDR holdings, reserve position in the Fund, and monetary gold) k = a compression factor of 0.95. The compression factor is applied to the uncompressed calculated quota shares, which are then rescaled to sum to 100.

Source: IMF documents.

However, the inclusion of the "openness" variable (O in Table 1) and the small weight given to reserves were against BRICS' preferences. BRICS were particularly concerned about the impact of openness because it primarily benefitted the Europeans, given intra-EU trade is counted as inter-country trade. Within-currency union trade, BRICS' Directors emphasised, was less likely to cause the kind of balance of payments crises facing countries trading outside of their own currency. For example, the Russian Director noted that, like their Indian counter-part, they could live with the openness variable only if "all intra-union trade was excluded during quota calculations" [IMF, 2002, p. 41]. This wish, however, was not met. Further, the BRICS' Directors would have preferred the weight on reserves as well as GDP PPP to be higher [e.g., IMF, 2007]. Despite these unfulfilled preferences, the 2008-2010 reforms nonetheless boosted the BRICS' voting power in unprecedented ways.

The same cannot be said of the 2008-2010 reforms at the World Bank. For example, as a consequence of these reforms, the rate of change in G20 emerging economies' voting power was 19 percent in the Bank, compared to 28 percent in the IMF [Kaya, 2015, pp. 172-173]. China's gains were twice as large in the IMF compared to the World Bank's International Bank for Reconstruction and Development (IBRD). The 2010 change to World Bank's shareholding formula, which officially de-linked World Bank shareholding calculations from the IMF's quota calculations for the first time, also fell short of BRICS' expectations. This formula consisted of three components: economic size, following the IMF blend of GDP (75%), "development contributions" (5%), and cumulative contributions to the International Development Association (IDA) (20%). Both the low weight of development contributions—a catch-all phrase of countries' input to the Bank's mission of economic development—and the high weight of the IDA contributions ran counter to the BRICS' interests. Not only have BRICS been relatively significant borrowers from the IBRD (as a proportion of the IBRD's total lending), they also contribute miniscule amounts to the IDA, whose primary donors remain the G7 countries (see Kaya, Chapter 6 for more detail). Nor did the BRICS end up seeing the reform they wished to see in IDA's donor-controlled governance. Another issue is the Bank is controlled relatively more from the top by a President, who has always been an American. In contrast, more of the IMF's senior management is now from BRICS, including a Deputy Director from China.

Voicing discontent with key policies

The picture has been similarly one of partial success when it comes to policy changes. Given space constraints, the pursuant discussions on this topic focus on the two issues most critical to the BRICS' preferences and the governance of the global economy: a) BRICS', particularly China's calls for change to the basket of currencies that make up the IMF's Special Drawing Right (SDR), and b) BRICS' calls for leniency on the use of capital controls within the IMF.

Case of the Special Drawing Right (SDR)

In November 2015, the IMF welcomed the Chinese renminbi to the basket of currencies that constitute the SDR, the IMF's reserve asset, with this decision to be implemented in October 2016. The SDR's original purpose was to provide relief from dollar-dependence in the Bretton Woods era of fixed exchange rates, when in the 1960s the supply of dollars (USD), which was tied to gold, was becoming tighter in the face of growing demand [e.g., Clark and Polak, 2002]. A basket of currencies (until

October 2016—the USD, the euro, the Japanese yen, and the pound sterling) determine the value of the SDR.[6]

Two main criteria have governed the inclusion of a currency in the SDR basket. First, countries/regions whose currencies qualify for the basket hold the highest ranks in terms of the value of their exports of goods and services. A 2000 decision limits the exports criterion to the currencies of the top four exporters [IMF, 2010a]. Second, in 2000, with encouragement from the staff, the IMF Executive Board decided to introduce a second requirement for qualification to the SDR basket —that a currency be "freely usable" (FRU).[7] Until the November decision, the latter of these criteria was seen as the impediment for the Chinese currency to enter the SDR basket.

BRICS, over the years, have requested re-evaluation of the SDR basket, with the eventual goal of revamping SDR's role in the international monetary system (IMS). Famously, in 2009 the Governor of the Bank of China, Zhou Xiaochuan, called for the creation of a "super sovereign" reserve asset to reduce IMS' reliance on the USD as the primary reserve currency, specifically pointing to the SDR to fulfil this key yet unclaimed role [Xiaochuan, 2009]. In 2011, at various platforms, the G20 emerging economies called for the IMF to reform the SDR to enhance its importance. They also argued that the inclusion of an emerging economy currency in the SDR basket could increase the attractiveness of the asset [IMFC, 2011; IMF, 2011a]. In a representative statement, the Brazilian Finance Minister emphasised, "[t]he SDR could play a larger role in the international monetary system, especially if its basket is enlarged with the inclusion of emerging market currencies" [Mantega, 2011]. At the same time, BRICS' summits have also emphasised the role of the SDR and its valuation.[8]

Initially, however, these calls were met with resistance from the dominant shareholders of the institution. For example, the 2010 IMF evaluation of the SDR basket commended China's efforts to liberalize the

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[6] The rationale of a basket methodology, which commenced in 1974, is to reduce volatility in the value of the SDR [Polak, 1979].

[7] Freely usable means the currency is widely traded and used in international transactions.

[8] See, for instance, Third and Fifth BRICS Summit Declarations (http://www.brics5.co.za).

international usage of the RMB, but found the currency to fall significantly behind the currencies in the SDR basket in terms of international financial transactions. In other words, the Chinese currency did not meet the FRU criterion, though by 2010 China had become the third largest exporter [IMF, 2010b]. Further, in 2011, Timothy Geithner, the US Secretary of the Treasury, downplayed the importance of the SDR: "[It] can't provide the role that many people would aspire to it, and there is no risk of" it replacing the USD [Geithner, 2011]. The European representatives were, similarly, resistant to change with an emphasis on the FRU criterion [e.g., Rostowski, 2011].

Eventually, however, BRICS' "voice" on the issue compelled several in-depth staff reports [e.g., IMF, 2011a, b]. The last one of these reports [IMF, 2015] reversed course on earlier ones, noting that the renminbi's (RMB) international usage, in trade and trading, had increased significantly, and the Chinese authorities were willing to improve impediments, such as access to financial markets on mainland China. The report essentially justified the extension of the SDR basket to the RMB, while at the same time committing China to further capital account liberalisation.

Changing views on capital controls

Until after the 2008 crisis, the IMF's general policy toward controls on inflows of capital was one of "stigmatization", seeing them as "harmful for economic performance, generating severe distortions, delaying policy adjustment and sending negative signals to market actors" [Chwieroth 2015, p. 52]. Indeed, in 1995 the IMF's Executive Board debated at length a staff proposal to endorse capital account convertibility as one of the IMF's mandates.[9] While different works disagree on the sources of this emphasis on capital account liberalisation [e.g., Abdelal, 2007; Chwieroth, 2010; Stiglitz, 2002], they converge on identifying it as a key area of IMF's advocacy of liberalisation.

[9] These discussions died out, as there was inadequate shareholder support to extend the IMF's jurisdiction, especially after the Asian crisis.

Yet, after 2010, the IMF's position on capital controls seems to have evolved [Gallagher, 2014]. For example, in a key 2011 policy paper, the IMF staff noted that "Emerging markets…are experiencing a surge in capital inflows…While inflows are typically beneficial for receiving countries, *inflow surges can carry macroeconomic and financial stability risks*" [IMF, 2011b, p. 3, emphasis added]. This shifting position culminated from a series of articles by IMF economists questioning the previously-held conventional wisdom in addition to years of pressure by emerging economies, particularly Brazil, but also China and India. In fact, BRICS pressed on this matter not just within the IMF, but also through other platforms. Importantly, in 2011 the G20 released "Coherent Conclusions" on capital account management, supporting the right to control inflows [*ibid.*, p. 11].

Although this shift in institutional stance was significant, it nonetheless did not go as far as completely meeting BRICS' preferences. For one, although BRICS preferred to not bring the management of capital flows under IMF surveillance, a 2012 shift within the IMF endowed the institution with powers to undertake surveillance on capital account movements [Gallagher, 2014, Chapter 6]. In other words, national autonomy was restricted in favour of multilateral guidance. At the same time, the Brazilian view of mutual-adjustment, where both capital sending and receiving countries had to take measures to decelerate the flow of cross-border capital was overlooked [*ibid*.].

14.4 Explanations

What explains these (partial) successes BRICS have had?

Credible Threat of Exit

One plausible answer appears to be their credible threat of exit. Randall Stone [2011], for instance, argues that the options a state has outside of the institution increases with greater economic power. And the more options a state has outside of the institution, the greater the willingness of the other members of the institution to allow the state to have exceptional sway over the institution. From this perspective, as the BRICS' economic importance has increased, so have their exit options. This point holds true even in the absence of the creation of new institutions. For instance, increasing economic fortunes have allowed BRICS to build up foreign exchange reserves, which in turn provide these states with self-reliance mechanisms during crises. In the presence of the increasing credibility of the threat of exit, if the current institutions are to retain their participation, then they need to heed BRICS' expressions of discontent. In Stone's words, the membership needs to "restore incentives" for the exiting state to "invest [back] in the institution" [p. 40].

Kastner *et al.* [2016, p. 171] also emphasise the importance of exit options: "China's favourable outside options, combined with perceptions of its indispensability on issues of global financial governance, provided China with the wherewithal to pursue a hold up strategy—a strategy by which China could make its cooperation conditional on concessions from other actors." Here, the aforementioned reforms are seen as the conditional "concessions". While the authors' exit argument is compelling and "hold up" is a pithy concept, it is debatable whether there was actual hold-up. Long before Congress had ratified the IMF reforms, China, and the other BRICS, had already provided credit lines to the IMF [Kaya, 2012], had consistently participated in reform discussions, and had conceded to reforms that did not meet their full demands. China had even agreed to voting increases below what the calculations had shown. Even more, whether the reforms were concessions per se remains debatable. The upshot is that from one perspective, the threat of exit compels increases to the BRICS' ability to rectify their discontent with the institutions. And, the institution's (partial) meeting of these demands, in turn, incentivizes them to cooperate in the institution.

Institutional factors

Analysing different issue areas, other authors have pointed to the importance of various institutional factors as well as the role of advanced economies, which act as institutional gatekeepers [e.g., Gallagher, 2014; Kaya, 2015]. For instance, the way in which the IMF is funded, with quotas and lending lines, demands more upfront contributions from shareholders than the way in which the World Bank is funded, since the IBRD can raise its own funds and the bulk of its capital is callable (drawn only when needed), which has never happened. Even more, since the IDA is donor-dependent with the advanced economies as its major donors and because these states are loath to forgo influence over it, there was little impact the threat of exit could make [Kaya, 2015]. In another example, the staff's changing views on capital controls, backed by new economic theories and research, has made them more amenable to the emerging economies' views on capital controls [Gallagher, 2014]. From this perspective, the institutional effects of underlying economic power will be contingent upon particular institutional characteristics [Kaya, 2015].

Negotiation Strategies

Another set of factors that could be considered is strategies for change [e.g. Kahler, 2013; Gallagher, 2014; Chwieroth, 2015]. Gallagher, for instance, notes that on the issue of capital controls, BRICS skilfully connected their demands for change in IMF policy to the academic shifts underway in the institution. And, the relatively unified voice of BRICS on critical financial governance issues eased their success with reforms. There are, however, remaining questions here. For instance, would even the best of strategies work in the absence of other factors, such as lack of willingness for change on the part of dominant states? Plausibly, lack of intra-group cohesion, poor timing, or institutionally irrelevant framings of voice can act as stumbling blocks even when the pathway to reform is relatively clear.

2008 Financial Crisis

One final factor is the 2008 global financial crisis, which has stressed advanced economies, thereby reminding the world of underlying shifts in economic power, and increased the demand for borrowing from the IMF and the World Bank. Rather than a cause for the particular changes, however, the 2008 crisis seems to, at best, explain their timing. Specifically, 2008 reforms at the IMF were foreseen in 2006, and the 2010 reforms were foreseen in 2008, but perhaps they could not be delayed beyond 2010 because of the IMF's need to replenish its coffers during the global crisis. A similar argument could be made in the case of the Bank.

In sum, the threat of exit needs to be coupled with institutional explanations in order for it to better explain success with voice.

14.5 Pathways to Exit?

Since the credibility of exit increases with alternative institutional options and because the extent to which these institutions are truly alternatives could signal pathways to exit (if not partial exit), it is important to analyse the institutions created by BRICS. This section's discussions on the AIIB, the NDB, and the CRA suggest that while these institutions are not truly substitutes of existing institutions, which would strongly point to exit [Hirschman, 1970], they nonetheless should be taken seriously as future pathways to exit, if BRICS' "voice" in current IFIs is stymied.

Asian Infrastructure Investment Bank (AIIB)

The BRICS' most significant institutional achievement stands as the AIIB, which in early 2017 had 57 members, 37 of which were from Asia. A widely-noted fact about the institution has been that a number of key American allies—including the UK, Germany, Australia, and South Korea— joined despite US officials' discouragement [Perlez, 2016].[10] The AIIB's main mission is to "promote investment" for "development of infrastructure", and it currently holds a capital stock of USD 100 billion (Articles 2 and 4 of the AIIB's Articles of Agreement (AA)). "Sustainable development" is the other primary goal of the institution. The institution is endowed with functions that are similar to the WB Group: it can directly loan or co-finance, make equity investments in an institution, guarantee loans, and provide technical assistance. Like the IBRD, it can buy and sell securities to raise funds (Chapter IV of the AA).

[10] G20 is not included as a BRICS accomplishment, since the transition from G7 to G20 was led by advanced economies.

The institution's structure also bears significant similarity to existing IFIs, with a Board of Governors composed of all members and a smaller Board of Directors (12 members, with 9 from regional members) as well as a professional staff. As in the IMF and the WB, as the numbers would suggest, while some members have their own Directors, other members share a Director under a constituency system. Also, as in the IFIs, voting power is weighted based on the member's capital subscriptions. China is the highest contributor (about 33% of the total capital) with the greatest formal voice (about 28% of the voting power).[11] Paralleling the IFIs, there are also "basic votes", which are distributed to members equally. Currently, the basic votes constitute 12 percent of the member's total voting power. Interestingly, this number is about the original share of basic votes in the World Bank (11%), and was the number aimed by a range of developing countries in the 2010 reforms [Kaya, 2015, Chapter 5]. In a further similarity with the WB, the AIIB has both paid-in capital (20% of the total capital) and callable capital (80% of the total capital, to be called upon in time of need) (Chapter II of the AA).

Another important similarity with the IMF/WB lies in the way in which the dominant member of the institution—in this case, China as opposed to the USA—exercises institutional power. As the institution's main architect, on decisions that require a "Super Majority" (two thirds of the vote representing at least three-fourths of the total voting power), China so far has de facto veto power. Recent statements by the AIIB President, Jin Liqun, however, have emphasised that China does not intend to use its veto and expects to lose it, as new members join the institution [Kynge and Pilling, 2017]. Given that US de facto power in the WB was retained throughout, this would be a novel development at the intersection of power and institutions. Further, the AIIB is headquartered in Beijing – the placement of the IMF/WB in DC has long been seen not just as a symbol of American dominance in the institutions, but also as a conduit for American informal influence over them.

The AIIB, however, also has some unique features. Noted as an "innovation" by some scholars [e.g., Chin, 2016], the organisation does not have a resident Board of Directors. The reasoning for this institutional

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[11] As of September 22, 2016, as reported by the institution.

feature was to speed up lending, in direct criticism of the cumbersome procedures of accessing the IMF and the WB. Existing research [Stone, 2011] shows that when there are greater levels of delegation (from the Directors to the management/staff), this actually provides more opportunities for the dominant shareholders of the institution to influence key policy outcomes, such as lending. Higher levels of delegation permit obfuscation of discussions pertaining to policy, providing an opportunity for the major shareholders to insert their (likely disagreeable) preferences without the prying eyes of the rest of the membership. Hence, existing research would suggest that the lack of a resident Board, all else equal, should make it easier for China to pursue its policy preferences relatively more effectively. Without adequate data on lending, however, this point remains theoretical, especially because principal (shareholder)-agent (staff) that plague other international institutions will also be relevant here [e.g., Hawkins *et al.*, 2006].

Indeed, more certainly, the lack of a non-resident Board suggests the staff's influence over the policy decisions. This is compounded by the fact the AIIB President, like his/her counter-part at the World Bank, holds a significant deal of sway over the institution. For now, the AIIB seems committed to hiring based on professional criteria – "an open, transparent, merit-based process", which means the training of the staff and the tendencies they bring with that training will be crucial variables to study in the coming years (AIIB AA, Article 30). It also appears that the selection of the President will be more open than the process at the World Bank. Until election of Jim Yong Kim in 2012, the WB's process did not include transparent interviews; whereas, the AIIB's Articles of Agreement foresees voting by the Board of Governors, though with a special majority [*ibid.*, Article 29].

The New Development Bank (NDB)

While the AIIB stands as the BRICS' most impressive institutional achievement, the NBD, which was India-initiated, shortly preceded it, having been launched at the 2014 Fortaleza Summit of the BRICS [Cooper and Farooq, 2015]. The NBD endorses the same mission as the AIIB:

investment in infrastructure and sustainable development. Yet, its membership is restricted to the BRICS. While originally China pushed for unequal contributions to the NDB, based on capacity to contribute, the other countries rejected this design with the fear that it would give China too dominant of a role [Kirton, 2015]. A compromise on China's part led to the institution being founded with USD 20 billion paid-in capital shared equally among its five members (ADB 2014). Like, the AIIB, NDB can provide financing in local currencies.

Contingent Reserve Arrangement (CRA)

During the Fortaleza summit, the BRICS also agreed on a currency swap arrangement worth USD 100billion to be activated in case of balance payments crises, which could take the form of either a precautionary credit line or an actual provision of liquidity. Brazil, Russia, and India pledged equal amounts of USD 18billion toward this arrangement, whereas China and South Africa promised, respectively, USD 41billion and USD 5billion. With its focus on crises and currency swaps, some could question whether this arrangement could replace the IMF.

Key institutional features of the agreement suggest that rivalling the IMF is likely not the CRA's purpose, nor is it in its capacity. First, the arrangement promises credit lines (see Article 1b of the CRA). Since states do not have to make assessed, mandatory contributions as in the case of the IFIs, their commitments are relatively lower. Second, only the BRICS are eligible to access these credit lines, which means that the institution will not be as multilateral as the universal IMF. Hence its capacity to provide financial stability as a global public good is restricted. Third, the IMF's technical capacity as well as its ability to dole out loans with conditionality remain attractive to countries, as the case of Germany's insistence on IMF's recent (2010, 2012) involvement with Greece shows. Fourth, CRA actually foresees IMF involvement. If countries want to access more than 30% of their maximum allowance from the reserve arrangement (which is a country-specific multiplier of each country's contribution), then they need to have an ongoing borrowing arrangement with the IMF (Article 5 of the CRA). Put differently, 70% of a country's access to the CRA is contingent upon an IMF arrangement, with which the country should be in compliance. In this respect, while the CRA may further reduce the already diminished chances of the BRICS' reliance on the IMF, it cannot be assessed as a truly alternative institution at this stage. Similarly, bilateral and regional currency swap agreements, such as Chiang Mai, are ruled out as alternatives to the IMF, even if their role in buttressing balance of payments crises for a short period is acknowledged [Kawai, 2015; Lin, 2015].

14.6 Explanations

What explains the BRICS' moves to create these new institutions, which can be seen as creating pathways for partial exit or as boosting the credibility of exit?

Institutional Gap

One explanation is the need to focus on infrastructure investment, which is inadequately met through current development institutions. Here, a number of BRICS, prominently China and India, have voiced the gap in infrastructure financing with particular references to the USD 8 trillion gap claimed in an Asian Development Bank study [Ming, 2016, p. 48; see also Chin, 2014]. From this perspective, then, inadequate provision of a quasi-public good has compelled a new leadership to emerge in the global scene. While such arguments about an "institutional vacuum" are important to recognise, BRICs' leading of the creation of new institutions cannot be explained by mere reference to it, since an explanation for why the vacuum was filled is pertinent.

Slow Reform at the IMF/WB

Perhaps the most widespread explanation for the BRICS' creation of new institutions has been the slow nature of progress on reform at the WB/IMF. Particularly, the significant lag between when the 2010 reforms were approved within the IMF and when they were ratified by the US Congress met with widespread public criticism (see above). Ben Bernanke, the former Chairman of the US Federal Reserve, for instance, remarked that "The US Congress is largely at fault for all that's happening [i.e. "exit"]", "The US Congress has not approved it. They should, they haven't…So I understand why other countries say, 'well let's take our marbles and go home'" [quoted in *Financial Times*, 2015]. David Dollar, a well-known expert on China and former World Bank official as well as an advisor to the AIIB, expressed similar sentiments, pointing to the inefficiencies in the Board-led loan diffusion by the WB as well as unfulfilled demands by BRICS for more infrastructure lending by the Bank [Dollar, 2015]. While the World Bank's cumbersome lending procedures could reasonably explain the emergence of the AIIB and its dedication to faster loans, the connection between the IMF and the AIIB seems a bit looser – a point which is further discussed below. Generally, however, failed reform lowers the cost of exit, since there is less to lose in (wholly or partially) abandoning existing institutional frameworks [Reisen, 2015].

Chinese ambitions

China's recently more assertive attitude could explain the creation of the AIIB and the NDB [Ming, 2016]. As Ming [*ibid.*, p. 44] notes, it is important to see these institutions as belonging to a "series of major policy initiatives adopted by the Chinese government to expand its influence overseas, including a 'Silk Road economic belt' and 'a 21st century maritime Silk Road'". Eswar Prasad of the Brookings Institution echoes this view, calling the AIIB "an instrument for China to lend legitimacy to its international forays and to extends its sphere of economic and political influence even while changing the rules of the game" [Quoted in Perlez, 2016]. It has long been noted that there is also prestige in pursuing a leading position in the international order [e.g., Gilpin, 1981].

Since state-specific goals (such as needing to attract infrastructure investment or the need to invest foreign exchange reserves) could be pursued bilaterally or an in ad hoc multilateral manner, China's efforts toward multilateral institution-building raises questions about the extent to which these institutions are challenging the existing, US-led multilateral order.

14.7 Challenges to the US-led Order

To the extent that BRICS have success with their voice in the existing institutions, they inevitably alter it away from the dominant members' preferences. This occurs by definition, since the existing institutions reflect the preferences of their creators relatively more.[12] For instance, while the AIIB promises to uphold labor, environmental, and anti-corruption standards, the traditional donors are reportedly concerned about these standards being eroded [Perlez, 2016]. The bigger issue, however, seems to be the one Gilpin [1981] raised decades ago: as new states gain economic power and as their capacity and ambition to alter the existing institutional equilibrium increases, a period of disequilibrium arises, followed by a new equilibrium under the newly dominant (i.e. formerly rising) states. The first part of Gilpin's theory seems to be materialising – the increasing economic prowess of BRICS is translating into bolder policy positions. But, disequilibrium is in the eye of the beholder. From the perspective of US officials and those wanting to see a continuation of US global institutional hegemony, it may seem like a disequilibrium, while it might be a much welcome and long-awaited shift in institutional rules and norms from the perspective of others that have lamented a US-dominated order.

Likely, the more immediate disequilibrium will be felt in Asia, particularly by Japan. Research has shown the negative effects of China's rise on Japanese influence at the Asian Development Bank (ADB) [Lim and Vreeland, 2014]. And, the AIIB's emphasis on regional cooperation and focus on infrastructure is more likely to immediately affect the ADB's actions and policies. Perhaps the Memorandum of Understanding signed between the institutions in May 2016, could be taken as a recognition of

[12] Notably, a diverse set of approaches in international relations – realism, liberal institutionalism, historical institutionalism – support this point.

this potentially uneasy co-existence.[13] Along these lines, some authors have argued that the creation of the AIIB indicates clearly that "China wants to assume regional leadership" [Hamanaka, 2016, p. 5].

Regardless, the success of BRICS-led institutions is yet unknown. In both the AIIB and the NDB, an important factor to watch is the institutions' borrowing and therefore lending costs, as BRICS face less developed financial markets, not fully convertible currencies with relatively shallow trading markets, and domestic institutional weaknesses [Reisen, 2015, p. 8]. Additionally, even though IFI reform and the global development/financial landscapes have been areas where BRICS have shown relatively high levels of coherence, there exist many plausible sources of potential conflicts between these countries, including: intra-group competition, China's perceived dominance of institutions and conflicting interests given the large economic disparities within the group. Further, the trade-off between looking inward to development needs and outward to international influence could intensify during economic downturns for BRICS.

Crucially, the IMF and the World Bank are still standing, and indeed the recent changes that BRICS sought and gained within them likely prolong their survival. Hirschman's original treatise on voice and exit emphasises this point: consumers who exercise voice are those that have decided– for now–to stick with the product. As Hirschman notes [1970, 83], the "threat of exit will typically be made by the loyalist—that is, by the member who cares—who leaves no stone unturned before he resigns himself to the painful decision to withdraw or switch." By the same token, however, to the extent that repeated efforts with voice go unsatisfied, not just pathways to exit, but actual exit can begin to emerge.

In any case, at the time of writing, arguably the largest challenge to the US-led post-war order seems to come from within the USA itself. A domestic backlash against globalisation has been building for years, including Congressional intransigence and more recently with the new Trump administration's nationalist economic policies. While such a state of affairs might be transitional, the long-term effects of it may not be. For

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[13] ADB, AIIB Sign MOU to Strengthen Cooperation for Sustainable Growth", May 2, 2016, www.adb.org.

instance, on January 24, 2017, reports of twenty-five new countries, including Canada, Ireland, and a couple of African countries, joining the AIIB surfaced [Kynge and Pilling, 2017]. If US abandons the leadership of existing institutions, where it is formally and informally the dominant member, or if calls for reforms fall on deaf US ears, then pathways for exit will strengthen and truly alternative institutions may emerge. The AIIB is providing a glimpse into that possible future.

14.8 New Research Frontiers on BRICS and IFIs

How can future academic studies expand upon existing analyses? One, it seems that the frontiers of research on BRICS and IFIs focuses on specific features of institutions and how BRICS' efforts for reform fare across different issue areas. For instance, research clearly identifies the issue of capital account liberalisation as an area where BRICS have had some success in achieving their goals for more autonomy on capital controls. It seems important to probe what made this area particularly suitable for success. As noted previously, existing studies provide a number of compelling explanatory factors, ranging from the shift in academic research within the IMF, to the smart negotiating strategies of BRICS, but more room remains for systematically exploring the interaction of these different factors. And, studies should analyse why and how BRICS failed to achieve similar levels of success in other issue areas.[14]

Second, and continuing with the theme of variation across institutional settings, it would be helpful to differentiate across the World Bank and the IMF more, instead of bundling them together. As noted here, BRICS have achieved more of their goals for reform in the case of the 2008-2010 reforms to the IMF than to the World Bank. While some studies [Kaya, 2015] argue this had to do with the constellation of a couple of key factors – the particular funding structure of the IMF being more state-dependent compared to the World Bank and the institutionally dominant states' greater interest in BRICS' involvement in the IMF—there is room for

[14] For the sake of disclosure, the author of this piece is currently working on such a book project.

more differentiation across the IMF and the World Bank. In particular, the World Bank faces an increasingly populated arena of development banks, with the recent addition of the AIIB and the NDB to a relatively long list of regional multilateral banks. It would be good to probe whether "regime shifting" is a greater possibility for the Word Bank than the IMF. Similarly, when discussing the effects of the rise of BRICS on the US-led order, it would be more fruitful to discuss uneven effects across different institutions within the order; rather than a single, uniform impact on the system.

Third, while "voice" and "exit" provide a compelling framework that mirrors actual developments pertaining to IFIs and BRICS (that is, the dominant story has been BRICS seeking reforms to ameliorate their discontent with institutions as well as bolstering their credibility of exit through new institutions), the interaction between these two phenomena need fine tuning in the literature. For instance, existing arguments that explain the formation of the AIIB and the NDB with reference to slow reform at the IMF are confusing institutional platforms, since AIIB and NDB have functions similar to those of the World Bank, not the IMF. More likely, the lack of adequate progress with "voice" during the 2008-2010 reforms at the Bank, in addition to grievances with Bank's lending procedures, spurred the creation of the AIIB and the NDB. Furthermore, even if the IMF could be taken to respond to any sort of exit (disengagement from the institution), it was not responding to the creation of the relatively small CRA, which came a few years after IMF reforms were undertaken in any case. Exit and voice are likely to co-exist and the translation of voice into desired outcomes is a lengthy process in multilateral institutions. Therefore, instead of trying to link the fulfilment of BRICS' demands for change to clear instances of (threat of) exit, it is more fruitful to raise questions about when voice, hence loyalty to the institution, will be abandoned. Finally, "exit for whom?" is a critical question that needs to be answered. There is a distinction between exit for one's self and exit for others. The only new institution studied here that may eventually offer an exit, an alternative, for others is the AIIB, given it is the only one with membership that extends beyond BRICS. In this respect, just as it is too late to declare the US-led-order-as-we-know-it is still intact, it is too premature to announce the dawn of a completely alternative multilateral order.

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