In South America there is an urgent need to improve growth rates, strengthen internal markets, and substantially improve the living standards of the population, in order to reverse migration patterns, achieve social justice, and reduce income inequality. Since 2006, several countries in Latin America began to consider the creation of a new alternative bank, “The Bank of the South”, that would utilize existing regional reserves to finance the development of its member countries. The Banco del Sur should strengthen regional integration; reduce asymmetries, poverty and social exclusion; promote employment; and activate a virtuous cycle of sustainable development, fundamental for the economic, social and political transformation of the region.

After a long process of international agreements, the Founding Charter of the Bank of the South was signed on December 9, 2007 in Buenos Aires by Presidents Néstor Carlos Kirchner (Argentina), Evo Morales Ayma (Bolivia), Luis Inácio Lula da Silva (Brazil), Rafael Correa Delgado (Ecuador), Nicanor Duarte Frutos (Paraguay), Tabaré Vázquez Rosas (Uruguay), and Hugo Rafael Chávez Frías (Republica Bolivariana de Venezuela). The Founding Charter can be found in the Annex of this document. (See Box 1 and Annex)

In the Founding Charter of the Bank of the South, the presidents of the Bank’s member countries agreed to define the Bank’s Articles of Agreement, structure and operational guidelines in 60 days (See Box 1). However, in November 2008, more than 300 days had passed, and the Bank’s Articles of Agreement remained unsigned.

What happened?

The delay has been caused by: 1) an inadequate working method, and; 2) differences in opinion among member countries.

There are several versions of possible Articles of Agreement proposed for the Bank of the South. What is needed is a new consensus. One should keep in mind that finalizing the Articles of Agreement is only a first step in creating a Bank. What is really important is not the Articles of Agreement but actually putting the Bank’s principles into action —hiring personnel, setting
up the organization and starting operations. At UNASUR meetings, the Banco del Sur is always mentioned, and is even colloquially referred to as BANSUR. Despite the lull in signing, countries in the region are still interested in the Bank. The big question is if member countries are going to agree on fundamental issues, or if there are seemingly insurmountable differences.

The Importance of the Bank of the South

It is fundamental to overcome differences among member countries and expedite the working method to create the Bank of the South. What is at stake is not only the creation of a development bank, but also a new regional architecture that entails three interrelated elements:

1. A Monetary Union of the South;
2. A monetary stabilization fund, the Fund of the South; and
3. A Bank of the South that utilizes existing reserves for regional development

South America is not alone in this attempt to change the international financial architecture from a regional perspective. The tough reality that all developing countries face is the current transfer of resources from the South to the North. Since 2000, instead of wealthy countries in the North transferring capital and development aid to the countries in the South, it is the reverse: unbelievably, poor countries finance rich countries, resulting in a negative flow of capital from South to North. (See Box 2) It is necessary to stop this flow. It is essential that the savings generated in developing countries are not used to finance consumption in the North, but rather invested in the development of Southern countries.

Asia with its Chiang Mai Initiative, the Middle East with its Bahrain Initiative and most recently Africa, are all embarking on processes similar to Latin America’s. It goes without saying that each region has its own limitations. In fact, an Asian currency is still not being used despite such being designed and ready to be operational since 2002. Until now, the Asian bond market has only served for public bonds and has not yet started to issue private bonds.

East is in an intermediate phase, with no hints as to when it may be put into practice.

Box 2. The South Finances the North: Net Financial Transfers to Developing Countries, 1995-2007 (select years, in billion dollars)
The Bank of the South will have a fund of collateralized guarantees for issuing bonds so that it can keep South American savings and international reserves circulating within the region. Thus, it is necessary for Latin America’s development that the Bank of the South moves forward, both in terms of policy space as well as for the additional funds it will provide to invest in the region. The time for this is now, when the financial crisis in the United States (US) is turning into an international crisis.

Problems with work methods

To date, the decision-making system of the Bank of the South consists of: 1) setting up Ministerial Summits; which are followed by 2) meetings of experts from the National Technical Commissions who implement the decisions taken by the Ministers of the member countries.

Given the tight agenda of the Ministers, particularly those from big countries, the first Ministerial Meeting after signing the Founding Charter on December 9, 2007 did not happen until 120 days later, on April 15, 2008, in Montevideo. Worse, only another Ministerial Summit followed after that, on June 27 in Buenos Aires, and it was called with such little notice that only four ministers could attend. As a result, the minutes from Montevideo have not been ratified by all countries.

The system of first having a Ministerial Meeting and later a meeting for the National Technical Commissions has proved to be slow and ineffective. It would be much more efficient and adequate to agree on some terms of reference, and to commission a technical team that would carry out the work without interruptions, to be be approved and/or modified later by the member countries. This is a normal working method used by multilateral development banks and regional organizations; it would speed up the process enormously.

Agreements on the Bank of the South

While the most difficult part, i.e. reaching a political consensus to create a Bank of the South, has been achieved, the technical aspects still have to be defined: How to build an alternative multilateral development bank and how to operationalize the principles of its Founding Charter in the context of a new regional financial structure? Latin America already has several multilateral development banks, including the Andean Development Corporation (CAF in its Spanish acronym) and the Inter-American Development Bank (IDB), but these have not served to activate a new development pattern in the region. How should it build a different bank?

Some consider that there should not be a difference between the Bank of the South and the rest of international financial institutions (IFIs), not understanding that what has impeded regional development is not only lack of financing but also the neoliberal policies imposed by Washington-based IFIs. This is the reason why Latin American presidents have opted to create a different bank – to win autonomy and ‘policy space’ to implement different development policies, new policies supportive of the region’s sovereignty and responsive to their citizens. The need for new policies is especially critical in light of the food crisis and imminent worldwide recession as a result of the North’s economic policies.

Though there have been important agreements on the Bank of the South, differences prevail.

In terms of the agreements, the capital contributions to the Bank of the South were approved at the Ministerial Summit in
Montevideo on April 15, 2008. Authorized capital was set at US$20 billion and subscribed capital at US$7 billion. (See Box 3)

The contributions, conditions of initial contribution and letters of credit vary according to which group a country belongs. In general, there are two groups: the first includes the wealthier countries (Argentina, Brazil and Venezuela) and the second includes the smaller countries (Bolivia, Ecuador, Paraguay and Uruguay). Overall, this allows total loans up to US$60 billion, theoretically giving the Bank of the South the same importance as Brazil’s National Development Bank (BNDES in its Portuguese acronym), which is the largest bank in Latin America despite being a national bank and not a multilateral bank. It has loans equivalent to $55 billion, which is greater than the World Bank loans in South America (US$36 billion), the Inter-American Development Bank (US$46 billion), and seven times more than CAF (US$8.1 billion)

The second and last Ministerial Summit in Buenos Aires focused on the areas of governance and administration. It was proposed that the Bank of the South be formed by a Council of Ministers (the Board of Governors in any other development bank), a Management Council (the Executive Board in the IFIs), the Council of Directors (which would carry out the day-to-day operations), and an Audit Council. Article V of the Founding Charter was ratified, accepting that the mechanism for decision-making in all bodies would be “one-country, one-vote”, in general. (See Box 4)

The proposed exception regarding the “one-country, one-vote” rule is in the day-to-day operations. Member countries strongly disagree on this. According to some of the Bank of the South management bodies, bigger countries believe that the Bank’s greatest contributors should have more vote in the Council of Directors. Specifically, they have proposed having more voice in operations greater than US$5 million, meaning practically all operations given that US$5 million is a small amount for the Bank. This discussion greatly complicates things, since a new bank should have a simple institutional structure and swift procedures. The idea has always been to keep administration to a minimum, instead of having complicated, different procedures at different levels, which would only generate a convoluted bureaucratic system for the bank.
Disagreements on Bank of the South

There are various disagreements, some already pointed out. Clearly, the realpolitik is different for a country like Brazil, which already has a powerful development bank, the BNDES, with a much larger investment portfolio than the World Bank. A quite different situation is that of the smaller countries, which desperately need funds for development. In a nutshell, the Bank of the South is about the big countries versus the small countries.

Following are some of the contentious issues and disagreements that have not yet been formally discussed in Ministerial Summits:

1. **Governability: “One country, one vote” or “one dollar, one vote”?** Currently, the lack of agreement is based on the interpretation of the Fifth Article of the Founding Charter, in which a democratic working system of one-country-one-vote was established. This system would be similar to the United Nations (UN), where each country has voice and vote regardless of how small it is, and fundamentally different from the multilateral development banks (e.g. the World Bank) where wealthier countries have the right to more votes given they contribute more resources. Of the countries that contribute most to the Bank of the South (Argentina, Brazil and Venezuela), only Venezuela backs democratic decision-making at all levels. Brazil and Argentina opt for a traditional multilateral bank model. Though they have agreed that the Bank of the South’s Councils should work under the one-country-one-vote principle, they consider that in the day-to-day administration the countries that contribute more funds should have more right to vote.

2. **Privileges and exemptions:** Some suggest that all bank operations, from procurement to investments and staff salaries, should be exempt from all kinds of taxes and custom duties. Others believe that this measure, which is copied from the IFIs, is inappropriate and in conflict with important efforts to fight tax evasion in the region. But this is only the beginning. The most controversial issue – spending – has not even been discussed yet. What investment policies will the Bank of the South give priority to? Will there be concessional loans, like in other development banks, and, if so, what will be the criteria for eligibility? Who will benefit?

3. **Funding:** Though the capital contributions of each member country have been agreed on, there is still no decision on the use of reserves, the origin of special concessional funds, co-financing, and other funding details for the Bank.

4. **Investment Portfolio: Should infrastructure be a priority?** Some countries insist on associating the Bank of the South with investment in infrastructure. However, Chart 1 shows how infrastructure is already the area with the most multilateral investment in the region, while areas in need of investment are social and agricultural sectors.2
The countries of the Bank of the South must address the food crisis immediately. According to the United Nations Economic Commission for Latin America and the Caribbean (ECLAC), the recent 15% increase in food prices has led to a rise from 35% to 38% in the number of people living below the poverty line. In just a few months, all the efforts to reduce poverty from 2002 to 2007 were obliterated. And poverty is not reduced with infrastructure. The Bank of the South’s loan portfolio should not be centered on big infrastructure projects alone, but rather on poverty and regional projects that reduce asymmetries, with a focus on social development and environment.

This certainly does not eliminate the possibility of investing in oil refineries, but environmental issues should be carefully addressed. Going a step further, the idea of sovereignty in different areas generates a completely different investment portfolio from those of the World Bank, IDB, and CAF. For example:

*Food sovereignty:* greater investment within the region, including agricultural reforms and increased income for farmers

*Economic sovereignty:* activities that promote Latin America’s productive capacity, generate decent work for all, and a tax base that may be used for community development

*Health sovereignty:* investment in cheap generic pharmaceuticals and universal access to medical services

*Sovereignty of natural resources:* in a way that profits/royalties may be used for public investment instead of as private earnings for big corporations.

5. **Eligibility by type of institution** – Should the Bank of the South finance large private companies? Though there is agreement that the Bank of the South will invest in financial intermediation for public national companies, small and medium-sized companies, cooperatives and social enterprises, some member countries object to financing large private companies. Others argue that it is necessary to distinguish between different types of large private business, some of which are important for Latin American society, such as companies that produce food, generic

**Chart 1. Multilateral Investment by Sector in Latin America, 2007**

![Chart 1. Multilateral Investment by Sector in Latin America, 2007](chart.jpg)
pharmaceuticals, fertilizers, etc. Others also argue the importance of promoting regional companies in order to reactivate Latin America’s economy.

The minutes from the Buenos Aires Ministerial Meeting hint at what is to come: “It was considered adequate that the Bank could provide loans to — in addition to the public, semi-public and mixed economy sectors — to cooperatives and the private sector, provided public sector’s approval. Venezuela believed the Bank should not finance the private sector, with the exception of cooperatives, social enterprises and communities.”

6. Distribution of investments among member countries and different terms of financing (concessionalism): Article I of the Founding Charter calls for a balanced investment among the Bank’s member countries. However, not all countries have the same absorption capacity. Furthermore, will all investments be made under the same conditions? Multilateral development banks offer concessional loans (or loans at softer terms and lower interest rates) and grants (free of charge) to countries with lower gross domestic product (GDP). This again generates a division between the larger and smaller countries, where in principle, smaller countries deserve concessional terms.

There are two options to avoid this division between countries. One is to keep different financing terms according to sectors (i.e., investments in the social sector could be concessional regardless of country/region, like the Venezuelan National Development Bank or BANDES does). Another option is the European Union (EU) model. Europe faced the same problem as Latin America of “big countries versus small countries” and resolved it by abandoning the idea of country, targeting concessionality to the poorest areas, regardless of what country they were in. In this way, it is not wealthier countries subsidizing the poorer countries (i.e. Brazil wouldn’t be subsidizing Bolivia), rather the wealthier regions subsidizing the poorer ones (i.e. the poorer regions in Brazil would also benefit from concessional financing terms).

7. Procurement: The Bank of the South’s Founding Charter indicates a preference for goods and services from the region. However, since there are only 12 countries in the region, the reality is that in some cases purchasing goods or services locally may not be feasible. In such a case, the following possibilities may be considered: a) One option is to allow purchasing of goods and services from non-Bank member countries, as long as they are provided by contractors from member countries; b) Another option is preferential treatment from other Southern countries, at certain price thresholds; c) A different option is untied procurement, open to any country in the world that offers the most competitive price. Clearly, there are trade-offs between supporting the South and allowing untied procurement.

8. Participation and transparency: Until now, civil society has defended tooth and nail the creation of an alternative Bank of the South, and it has been a positive force. However, there is no agreement on its possible inclusion in the Bank of the South. The level of civil society’s participation is one of the disagreements among various member countries. There are several
The Reality of Aid

institutional models, analyzed in other documents, which should be contemplated before taking a final decision.

9. Social and environmental safeguards: How can it be assured that the principles in the Bank of the South’s Founding Charter, with the objective to promote socio-environmental justice, are maintained? Multilateral development banks have developed a series of social and environmental safeguards, created to maximize positive impacts in employment, distributional impacts in gender, generations (youth, older persons), ethnic groups and persons with special needs, as well as in environment. However, many of these safeguard policies are currently being watered down, given the IFIs’ move towards more conservative policies. For the Bank of the South, the challenge is how to incorporate these safeguards in a simple manner, without creating excess paperwork, delays and bureaucracy but ensuring the abandonment of the orthodox development model that brings about greater social exclusion and destruction of the environment.

In light of all these small disagreements, the Ecuadorian government asked the UN for assistance in the beginning of 2008. A non-binding Technical Workshop was held in Quito, on June 23 to 27, 2008. More than 60 people from different affiliations participated in this meeting: international experts in banking and finance, academics, members of Bank of the South National Technical Commissions, and civil society. The debate was intense; precisely, the intention was to analyze options, their advantages and disadvantages, and reach a consensus on building an alternative multilateral bank.

The resulting document is not a new proposal, but rather a presentation of the pros and cons of different options in the areas of: (i) Governance and Administration, (ii) Funding Resources, (iii) Investment Policies and Lending Framework, (iv) Procurement, (v) Audits, (vi) Operational Cycle, (vii) Participation, and (viii) Social and Environmental Safeguards.

The document may be consulted in the attached link, it is designed to assist in drafting the Articles of Agreement as well as the Bank’s Operational Guidelines: this will require deciding among the different options in each area, which are presented in a neutral form to help generate consensus.

The Bank of the South Must Move Forward

The Bank of the South advances so slowly that the delay is generating impatience. Another regional alternative development bank is forming: the Bank of the Bolivarian Alternative for the Americas, or ALBA Bank, to support regional integration between Bolivia, Cuba, Honduras, Nicaragua and Venezuela. The ALBA Bank has US$2 billion in subscribed capital and already has offices in Caracas. This is another path and does not involve UNASUR members, except Bolivia. Given delays, last August 29, 2008, the presidents of Venezuela and Ecuador agreed on the creation of a development bank for Bolivia, Ecuador and Venezuela, notwithstanding their support to promote the Bank of the South. This is undoubtedly a way to create pressure on the
bigger countries. In Buenos Aires, they assure that the Bank of the South will be operative before the end of 2008. In Brasilia, this is less clear given BNDES exists.

It is essential for the Bank of the South to begin operations even if in its smallest expression and thus be able to start issuing bonds in the South American monetary currency unit. Payments in national currency for intraregional trade have already been agreed upon and in the next UNASUR Ministerial Meeting, they will finish widening the use of national currencies. The next logical step is to start using the South American basket currency as a reference unit. The South American monetary unit was presented in a conference of central banks in Buenos Aires in August 2008, and later in Mexico in October 2008.\(^6\)

The construction of the European monetary system took six years in its first efforts, however, reasons to speed up in Latin America are evident, in light of the South to North transfers and the global financial crisis. For this reason, the Bank of the South should be born as soon as possible, together with its sister institution, the South Stabilization Fund that seems to be taking form with the recent agreement in Basle of Mexican, Brazilian, Argentine and Chilean central banks to jointly manage the international reserves.

Let’s look at the counter-argument: What would happen if the Bank of the South was not consolidated due to petty differences between member countries and an inadequate working method? This would enormously benefit Northern countries, which would keep receiving Latin American savings. This would also greatly jeopardize Latin American people who would continue to live in economic instability, precarious employment, food insecurity, and limited social progress.

For these reasons, Latin American countries must urgently try to reach a consensus: it is better to have an imperfect bank than no bank at all. However, if it is a mere replica of the IFIs of the current multilateral development bank model, Latin America would lose a historic opportunity, important not only for the region but for many other Southern countries that are watching this experience with hope. The Bank of the South must go ahead.

---

**Dr. Isabel Ortiz** received her Ph.D. from the London School of Economics, and has over 15 years of experience working in 30 countries in various areas of economic and social development. From 1999-2003 she was Senior Economist (Poverty Reduction) in the Strategy and Policy Department of the Asian Development Bank (ADB). Ms. Ortiz has also been a lecturer and researcher, publishing in Europe, Asia and the US. Recently she has worked with Nobel Laureate Joseph Stiglitz’s Initiative for Policy Dialogue.

**Dr. Oscar Ugarteche Galarza**, is Peruvian, with a Ph.D in History and Philosophy of the University of Bergen, Norway; M.Sc. of the School of Business of the University of London; and graduate of Finances in the School of Administration of the University of Fordham, New York. He is a member of the Institute of Economic Investigations (IIIEC) of the Universidad Nacional Autónoma de Mexico (UNAM) and Coordinator of the Economic Observatory of Latin America (www.obela.org). He is a member of the National System of Investigators of Mexico and an advisor of the Latin American Network on Debt, Development and Rights (LATINDADD).
Endnotes

1 Isabel Ortiz is a former senior official of the Asian Development Bank and Oscar Ugarteche is a researcher at the Economic Research Institute of the National Autonomous University of Mexico. The opinions expressed in this article are the authors'.

2 Annual Reports from the Inter-American Development Bank (IDB), World Bank, Andean Development Corporation (CAF) and webpage of the Initiative for the Integration of Regional Infrastructure in South America (IIRSA).

3 ECLAC. August 2008: Economic Survey of Latin America and the Caribbean. Santiago, Chile: United Nations Economic Commission for Latin America and the Caribbean


5 See: http://www.elcomercio.com/noticiaEC.asp?id_noticia=218399&id_seccion=6

Annex

Bank of the South Incorporation Agreement Signed
*Oscar Ugarteche (Translated by Suzanna Collerd)*

Finally, twenty months after the Bank of the South was founded in Buenos Aires, the South American presidents signed the incorporation agreement of BANCOSUR in Porlamar, Isla Margarita, Monday, September 28, 2009. Commissions from financial ministries negotiated the regulations of the incorporation agreement, clarifying capital contributions, the voting mechanism, personnel recruitment, jurisprudence, tax and legal considerations for officials and the bank’s function. What it is for, exactly?

The Initial Declaration

The Bank of the South is full property of UNASUR’s ten member countries. Venezuela and Argentina initiated negotiations for its constitution in 2006; later Ecuador and Brazil joined in May, 2007 and finally all members signed. As opposed to the Andean Development Corporation (CAF), with 18 member countries, some from Central America and others from other continents, BANCOSUR is South American in its essence. In this way, Chile’s position as an observer, although consistent with its position on Latin American integration since it withdrew from the Andean Pact in 1977, is a disadvantage compared to its small-scale, $21 million dollar participation in CAF. Even though this amount is minimal, it shows their presence. Currently, there is no such demonstration of presence with this bank. This is reminiscent of British foreign policy toward European Integration when it remained an observer during the decades of the European Economic Community’s formation; even after Europe’s integration, the British maintain an autonomous immigration policy and keep their tender. The English were not going to allow Continental Europe to dictate their monetary or immigration policies.

Colombia, for its part, has played an ambivalent role. Initially, it rejected the idea in 2006, but later expressed its agreement in the second half of 2007. Nevertheless the day before the signing Colombia withdrew; this produced confusion in the founding document because eight countries appear, but there are actually only seven signatures. Peru is the only South American country unreceptive to this idea, although perhaps the next government will decide to incorporate. It seems that this opposition is because of Venezuela’s predominant role in the bank and the close friendship between president García of Peru and Venezuelan former president Carlos Andrés Pérez of the fallen Democratic Action Party. Therefore, Peru’s absence shows a lack of formality in its foreign policy. Also, Peru is not an active participant in UNASUR as shown by the presidential absence in Margarita Island on the weekend of September 26th and earlier in Santiago, Chile.
Peru and Colombia play alongside Washington and commit themselves to the policy based on bilateral agreements championed by the former president of the United States. Both countries seem to lack an integrationist foreign policy and concur with Washington’s policy of divide and conquer, based upon the understanding that the winner in regional integration is a country whose government is not of their liking. Thus in UNASUR and BANCOSUR they play the same role they did in the club of debtors at the peak of the debt crisis in 1984, whose constitution failed in May of that year because these two countries served as a conduit for Washington’s opposition. This according to the renown work of Ambassador Alzamora Valdéz, then Executive Secretary of the Latin American and Caribbean Economic System (SELA).

The Signing of the Incorporation Agreement

In the context of a meeting between presidents of South America and Africa, seven out of the eight attending South American presidents (Hugo Chávez of Venezuela, Luiz Ignacio Lula da Silva of Brazil, Rafael Correa of Ecuador, Fernando Lugo of Paraguay, Evo Morales of Bolivia, Cristina Fernández of Argentina and Tabaré Vázquez of Uruguay), signed the incorporation agreement of the Bank of the South, founded in Buenos Aires the day before the swearing in of Cristina Fernández in December 2007. It took 20 months to do what was then promised would take 60 days according to the sixth point of the foundation agreement. This process has been much faster than that of the multilateral fund of ASEAN that took 9 years to be constituted in May of 2009, or the European institutions that took decades. Now, as in 2007, Colombia did not sign in and Peru was not even in the picture.

Throughout these two years it was agreed that the bank will start with a total capital of $7 billion dollars and that each country will have one vote in the board of directors as well as in the credit council for credits of up to $70 million. For larger credits the voting will be proportional to capital contributions. The three big countries and the four smaller ones will pay these contributions in different proportions. The latter will pay $400 million dollars each.

The initial outstanding capital is $7 billion dollars, double that of CAF. The authorized capital of CAF is $10 billion while Bank of the South’s is $20 billion as president Chávez announced. The outstanding capital of $7 billion will be contributed to the bank in the following months to begin personnel recruitment. The idea of the Bank of the South is that it will not focus on infrastructure, like the CAF and the IDB, but on projects to close the poverty gap in the South American region.