THE BRICS AND THE REFORM OF THE INTERNATIONAL INSTITUTIONS[1]

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INTRODUCTION – Historical Background.

I have organised this presentation in the following format:

i.- This INTRODUCTION – Historical Background;

ii.- The doctrine of oppression and the ideology of the crisis;

iii.- Neo-liberalism and the developing economies;

iv.- The rich countries and the collapse of the markets;

v.- The BRIC countries and their emerging role in international relations;

vi.- Some reflections on the reform of the international organisations; and

vii.- Conclusions – some scenarios.

The world order that emerged from the Second World War, in 1945, reflected the power profile of the countries in the world stage at that moment, particularly in the political arena, with the adoption of the charter of the United Nations (UN), on the 24th of October, 1945. In the decision structure of the new body, the more democratic option of a majority vote by the General Assembly was eschewed in favour of a Security Council in which 5 States (China, France, United Kingdom, United States of America - USA and the Union of the Soviet Socialist Republics - USSR, now the Russian Federation) had a veto power.

This undemocratic ethos of the UN, proposed by the then US president, Franklyn Delano Roosevelt, at the Tehran conference of 1943, was a very bad start for the organization, particularly because the war had been fought in the name of democratic values by the western states, in

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[1] Basic text of the speech given at the Law School of the Central University of Political Science and Law, Beijing, China, on the 27th of October, 2009.

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accordance with the Atlantic Charter of 1941, agreed upon by the British and U.S. leaders[3].

The situation of control was not much different in the other international institutions created after the war as a consequence of the so-called Breton Woods conference, with the exception of the fact that the western powers took all institutional power in them. Accordingly, both the International Monetary Fund (IMF), designed to regulate and supervise international transfers and payments, and the World Bank, created to supply credit for the reconstruction of destroyed economies, admitted vetoes by the USA, and the division of leadership, an American citizen for the World Bank and a European for the IMF.

In matters of international trade, the framework of the respective multilateral convention, the General Agreement on Tariffs and Trade (GATT) of 1947, was entirely set up by the US and British negotiators and enshrined a reversed veto in the consensus mode of deliberation, by which any changes to the structure would need to be approved by all. The creation of a new institution in 1995, the World Trade Organization (WTO), at the end of the Uruguay Round of the GATT, only preserved the old vices[4].

Thus, the post-war world order served basically to promote the prosperity of a few western states, notably the USA, and its global geo-political interests, particularly against those in opposition from the USSR, in the political confrontation which became known as the cold war. Developing countries at the time became merely puppets in the struggle for hegemony. It must be said that the mere existence of the USSR prevented a renewed colonialism by the hegemonic western states, deeply engaged in the thorough, methodical and merciless exploitation of the developing countries.

The doctrine of oppression and the ideology of the crisis.

This was so because the ideology inspiring the international action of the hegemonic capitalist nations was based on a number of prejudices which included the supremacy of the white man, the superiority of one country with a manifest destiny, the prevalence of the interests of the individual over those of the society in general, and the sanctification of greed as a force of social organization.

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[3] Rees, Laurence, Behind Closed Doors, BBC Books, London, 2009, Page 122.
[4] Goyos Jr., Durval de Noronha, Arbitration in the World Trade Organization, Legal Observer, Miami, 2003, pages 122 *et seq.*

Of course, many of the elements of such prejudices and guidelines existed for centuries and served many forms of exploitation of the weak by the strong. It was, however, only in the 19th century that attempts were made to transvestite the rapacious and brutal actions of the exploiters in the respectable garments of economic theories.

In the beginning of the 80s, notably after the fall of the Berlin Wall in 1989, and the end of the USSR in 1991, the economic doctrine of neo-liberalism, as conceived by Professor Milton Friedman, of the University of Chicago, USA, became prevalent in the developed countries, who sought to disseminate it in the rest of the world to their advantage.

Milton Friedman, who received a Nobel Prize in 1976, wrote the book Capitalism and Freedom, published originally in 1962. He taught generations of economists from many countries, influenced the formulation of economic policies of Margareth Thatcher (1979-1990), in the United Kingdom, and of Ronald Reagan (1981-1989) in the USA. He also inspired the adoption of economic and financial policies by international institutions with a view to promoting the selective prosperity of a few developed countries to the detriment of the vast majority of the world's population, living in the developing countries.

His doctrine, which came to be known internationally as the Chicago School was, in reality, a primary, anachronistic and radical view about economic liberty as a means in itself, a self-fulfilling exercise. Moreover, the almost absolute economic freedom would be the adequate manner of achieving the political liberty for all.

The mere capitalist competition would promote political freedom and answer the demands both from the market and society, because the voluntary cooperation of individuals in competition would promote the coordination of millions of persons. Thus, the only remaining ethical problem would basically be what an individual should do with his freedom.

Thus, by removing the organization of economic activity from the control of political authority, the market eliminates this source of undesirable coercitive power. The market permits unanimity without conformity and is an effective means of proportional representation (*sic*). Accordingly, consumers would be protected by the mere presence of alternative product providers and not by the action of the State.

According to Friedman, the neo-liberals do not advocate anarchy, since they contemplate a role for the state, even if a minimalist one, for the purposes of enacting rules, mostly for the purposes of defining and guaranteeing property rights and creating the means of payment, i.e., a monetary system. Similarly, it is incumbent upon the state to act as an arbiter in the disputes among individuals, companies and the sundry economic agents.

However, the neo-liberals do not see a role for the state intervention in the economy, not even as a promoter of economic activities by means of public expenditures with a view to the development of infra-structure, the creation of jobs and investments of social impact. In a capitalist society, according to Friedman, it is only necessary to convince a few rich people to raise funds to launch any new idea, even if a disparate one.

In this manner, the role of the state should be very limited and many traditional actions of government should be abandoned. Public education should be avoided in favour of private schooling. Government efforts towards a national health service and a pension programme should be abandoned.

The minimum wage should be abolished, in the same way as any regulation of industry and the state control of radio and television. Any and all regulated activities, such as the legal professions, should be liberalised. No public housing system would be justified, as private initiative is perfectly capable to provide ample housing for the population at large.

The state should not get involved in the creation of parks or national reserves or even in the construction of public roads. The mail services should be exclusively private. The market would provide all with greater efficiency, greater liberty and without coercion to the citizens of a country.

In the financial area, the state would act better in the creation of rules rather than acting as an authority. The role of the central banks should be minimalist, if at all justified, considering that money is too serious a value to be left for central bankers. Exchange controls should be abolished and currency exchange should be floated, as the market will better define the adequate threshold between two currencies in the basis of offer and demand.

Friedman ignored greed, this important component of human nature, in the formulation of his theory. Thus, competition rather than promoting cooperation strives for the elimination of the rival, dominance of the markets and imposition of ones own terms, however harsh, on the consumers. Thus, Friedman's proposition that unrestrained competition is an efficient means of social organization is not to be taken seriously, unless it is employed as a means of a cruel and rapacious exploitation of the many by a few capitalist individuals.

In addition, Friedman conceived his theory based in the observation of economies still fundamentally based on industrial activities and the international trade of goods. He erred dramatically in not foreseeing the disaster in making of economies based almost entirely in unregulated and grossly inflated financial markets, which are dissociated from the economic reality[5].

Neo-liberalism and the developing economies.

Therefore, if in the domestic economies, Friedman's construction can be identified as the ideology responsible for the financial crisis of 2008, in the international area it was incorporated in the measures itemised in the so-called Washington Consensus, which inspired the relevant multilateral institutions to assist developed countries in the organised plunder and exploitation of the developing nations.

The nature of the detrimental action of the multilateral institutions towards developing countries was recognised even by economists belonging to the system. One of them, Joseph Stiglitz, observed that "…part of the problem lies with the international economic institutions, with the IMF, World Bank and WTO, which help set the rules of the game. They have done so in ways that, all too often, have served the interests of the more advanced industrialised countries – and particular interests within those countries – rather than those of the developing world[6]."

The Washington Consensus induced the developing economies to i) raise their interest rates, so that capital could be abundantly remunerated; ii) raise artificially the exchange rate of the respective currencies in a way to cheapen the cost of imports; iii) reduce dramatically their tariffs, in order to facilitate market access to imported

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[5] Goyos Jr., Durval de Noronha, Diário da Crise, Observador Legal Editora, São Paulo, 2009, Page 119 *et seq*.
[6] Stigliz, Joseph, Globalization and its discontents, The Penguin Press, London, 2002, page 214.

products; iv) privatise their state companies; v) eliminate subsidies; vi liberalise the foreign capital legislation and remittances abroad; vii) deregulate the financial markets; viii) eliminate subsidies; ix) promote a tax reform with a view to reducing the tax revenues; x) promote fiscal discipline, with a view to minimise public expenditure; and xi) provide legal security to property and to foreign investment.

In most developing countries around the world this infamous recipe for exploitation by the rich economies was put in practice with disastrous results in the case of some Latin American countries such as Argentina and Mexico. Others, like Brazil, stopped the exercise mid-way as a result of elections favouring governments more compromised with the national interests. However, their economies remained closer to the industrialised and agricultural sectors than to the vaporous financial markets, even if there was a great denationalisation of the banking sector in Argentina, Chile and Mexico.

This tendency was not observed in countries such as China and India, for a number of reasons of internal order. It is indeed admirable that China succeeded in maintaining the substance of its development model even after the 15 years of hard negotiations that ultimately led to its accession to the World Trade Organization on the 11th December 2001. The modifications in about 9,000 laws and regulations that preceded accession to the WTO not only did not alter the core of the Chinese development policies, but also allowed for a modernisation of its legal infra-structure.

Thus, the joining of the WTO allowed China the protection of the most-favoured nation clause (MFN clause) to eschew the discrimination in the international commerce of its products permitted against non-members of the multilateral trade system at the same time it made the domestic legislation more attractive for direct international investments, including joint-ventures.

In addition, for many years, China was neither a member of the IMF nor of the World Bank and traditionally saw with guarded reserve and diffidence, to say the least, the advice and or recommendations of such international bodies and the respective sources of inspiration in the private initiative of the hegemonic countries.

Because the USSR had opposed this model until the foundation of the Russian Federation in 1991, the recipes designed to explore the rest of the developing world never set deep roots in its legal system. Until today, Russia has not joined the WTO, which allows disgraceful discrimination against the country, for the reasons already explained. This is due to opposition from some developed countries seeking immoral gains for the respective private sectors, notably in the oil field.

On the other hand India, a country that became independent of the infamous British rule only in 1947, had much to reconstruct of its destroyed economy by the chaos of the colonial administration, and adopted a very conservative economic model, close to the basic needs of its people and prioritising generalised social development.

The rich countries and the collapse of the markets.

It was in this background scenario that the world witnessed the eruption of the acute phase of the financial crisis in September 2008, with the collapse of the leading US investment bank, Lehman Brothers. By the end of 2007, the unregulated trade in derivatives had reached the unbelievable amount of US$ 600 trillion, against a volume of US$ 80 trillion in 1998.

The disparate nature of such numbers become evident when compared to the value of the world's Gross Domestic Product (GDP), the total market value of all final goods and services produced in a country in a given year, of about US$ 50 trillion in 2007. In the same year, the GDP of the USA was of about US$ 15 trillion; that of China was approximately US$ 3 trillion; and that of Brazil close to US$ 1.2 trillion. That very year, the total value of the international trade in goods was of approximately US$ 13.6 trillion.

Abuses in the trade in derivatives, particularly those based on real estate underlying transactions, had already been the determining cause of the Great Crash of the markets in 1929, which brings us to evoke the lessons of F. Hegel to the sense that experience teaches that men and governments have never learnt anything from history.

In any event, the financial crisis hit the USA with an enormous impact force in view of the degree of the leverage of the markets, as we have seen, in a moment of an accentuated weakness of the macro-economic fundamentals of that country. In accordance with data from the Federal Reserve, the accumulated debt of the federal government, states, financial sectors, businesses and households reached about 350% of the US' GDP[7].

By the end of 2007, the trade deficit of the USA was already US$ 820 billion and the country's current account deficit was about US$ 752 billion, or about 4.8% of the country's GDP. To this amount, military expenditures of the order of US$ 600 billion should be added. Thus, the country had become extremely dependent on investments by some of the cash rich developing countries, such as Brazil, China and Russia, in its government bonds.

This only became possible because the US dollar is still today, the main currency reserve in the world, which means that countries apply their reserves in US bonds and most of the international trade is conducted in this currency. According to data from the IMF, about 62% of the international reserves in 2008 were denominated in US dollars, 27% in Euros and 11% in other currencies such as the Yen and the Pound Sterling.

However, once the markets collapsed in September and October 2008, the US government announced disbursements of subsidies of more than US$ 1 trillion for its financial sector, in what it was followed by the United Kingdom with US$ 750 billion, by Germany with US$ 500 billion and by France with US$ 450 billion. In addition, all such countries, acting without cooperation with any of the multilateral institutions, disbursed direct subsidies to many of its industrial sectors, such as the automotive.

For 2009, it is estimated that the USA will compromise about US$ 2 trillion in sundry measures for its financial and non financial sectors, which correspond to approximately 13% of the country's GDP. This year alone, more than 100 banks of a small and medium size collapsed in the USA, whose depositors had to be rescued by the Federal Depositors' Insurance Corporation (FDIC), which became illiquid in the process, as its resources are no longer sufficient to cover the risks involved.

As a result, the frailty of the US dollar became apparent to all and so its inadequacy to serve as a reserve currency on which the world economy could be anchored. Even the Central Intelligence Agency (CIA) presented the extraordinary forecast to the effect that the US dollar would lose its reserve status by 2025[8].

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[7] Wegelin & Co, Investment Commentary number 265, August 24, 2009.
[8] O Novo Relatório da CIA – Como será o mundo em 2025?, Editorial Bizancio, Lisboa, 2009, page 83.

Other observers nearer to the realities of the financial world, however, see the date of the end of the hegemony of the US dollar as much closer. Some estimates put that date as near as 2011, "as the US economy will deteriorate into 2011 as the effects of excess consumption and the financial bubble linger", as stated by the economist of Sumitomo Mitsui, Japan's third largest bank[9].

The BRIC countries and their emerging role in international relations.

On the other hand, the BRIC[10] countries have not only approximately 50% of the world's population, are perceived as the leaders of the developing countries because of their benign foreign policies, in great part co-ordinated for quite some time, are now the main engine of the world's economic development, but also have joint reserves in foreign currency today amounting to approximately US$ 3 trillion.

Thus, the rich countries are now heavily dependent on the developing economies of the BRICs. This is so not only for the continuation of the activity levels of the world's real economy, but mostly for the support of the stability of their reserve currencies, particularly the US dollar, without which their financial markets, which account for most of their GDPs, would collapse.

It is not only the US dollar that is in danger as a reserve currency. The British pound has also lost substance, as the fiscal macro-economic profile of the British economy deteriorated with the financial crisis, the ensuing recession, the worst since 1955, and all that in spite of the massive subsidies disbursed in the past 12 months, which account for about 50% of the GDP of the United Kingdom.

Even for those who see with no sympathy the history of the developed countries, their imperialistic approach and the devastating effect their policies have had over the majority of the world's population, a sudden collapse of the US dollar should be seen with grave preoccupation, as it would undoubtedly cause an economic depression without precedents and one that would affect the whole human kind. One should also not discard the possibility of military conflicts in the aftermath of such an event.

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[9] Dollar to hit 50 Yen, Cease as Reserve, Sumitomo Says, bloomberg.com, October 15, 2009.
[10] Acronym for Brazil, Russia, India and China.

It must be recognised that, at this moment, the BRIC countries offer no real alternatives for a reserve currency. Of the four nations that form up the BRICs, only Brazil has a convertible currency, which is now very stable and has appreciated, this year alone, about 40% against the US dollar. However, the Real is not today in a position to become a major reserve currency.

Thus, for the BRICs, it would seem that only a major reformulation of the international institutions would permit to protect their economic and financial interests, as well as those of the remaining developing countries. Such reforms would permit the world economy to avoid the very present risks of extraordinary downturns.

Of course, for the bankrupt rich economies, it would be of interest if their now value deprived currencies were still supported by all. This would permit such countries to borrow in their own currencies and to print more money, as necessary, for the repayment of their debts. However, this latter model is untenable, as it would only postpone a major currency crash.

Some reflections on the reform of the international organisations.

These ample reforms, which are now required, should of course and in the first place, create a more balanced and democratic order at the UN. These should target at the elimination of the decision process centred on the Security Council, the eradication of the permanent seats and the total abolition of the veto powers. Accordingly, the relevant decision powers should be shifted to the General Assembly, with votes possibly weighed by population of the respective members of the UN.

At the IMF, the BRIC countries are at this moment grossly underrepresented, holding collectively only 10% of voting power, compared to about 32% held by the EU and 17% by the USA. Brazil has about 1.5% and China has approximately 3%. As the quorum of deliberation at the IMF is of 85%, the USA has today a very effective veto power at the organisation.

Commenting on the current situation of governance at the IMF, the Deputy Governor of the Chinese Central Bank, Yi Gang, declared in Istanbul at the annual meeting of the organization, that “the long-time underestimation of the quota share of the emerging markets and developing countries and their insufficient representation in the IMF are major causes for irrational governing structure, unfair surveillance and untimely early warning system[11]." Brazilian and Russian authorities have made declarations to the same effect[12].

A major and urgent measure to be undertaken by an IMF post-reform would be, of course, the creation of a reserve currency or means to substitute the US dollar in an orderly faction, with a view to maintaining the world's economic activities sustainable and free of the potentially devastating consequences of a sudden collapse of the US tender.

In addition, an IMF post-reform should be enacting regulation with a view to curbing the abuses of the international financial markets, as we have seen in the recent past. There is a trenchant necessity of consolidated international regulations, otherwise any restrictive domestic measures could be easily circumvented, if not defrauded, by the usage of more lenient markets to the detriment of those regulated.

Moreover, an IMF post-reform should be supervising the financial markets, the banks and investment banks operating internationally and the ancillary players, such as rating agencies, bankers (and their respective remuneration), financial advisors, auditors and lawyers working in international monetary and financial operations.

In the World Bank, the situation of under-representation of the emerging economies is the same as in the IMF. As it is structured today, the World Bank does not attend to the interests of human kind, because of its distorted doctrine, because of its failed leadership, because of its inadequate resources, and because of its corrupted power basis.

In a recent report, a high level commission of the World Bank declared on October 22, 2009, that "the world needs a World Bank which reflects the economic realities of the 21st century and which is financially sound, capable of supporting its clients through the recovery and into the post-crisis era. Action on voice reform and on capital should not be delayed[13]".

However, recent reforms proposed by the current president of the World Bank, an American, like all the other leaders of that organization

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[11] China urges IMF quota share adjustments, China Daily, October 5, 2009.

[12] Países europeus resistem em abrir espaço para emergentes no FMI, O Estado de São Paulo, September 25, 2009.

[13] Give greater say to emerging economies in World Bank, China Daily, October 23, 2009.

since 1944, only contemplate giving developing countries 47% of the voting shares in the institution[14], which is not sufficient for the implementation of the much needed shift towards decency.

Traditionally, the World Bank has been the financial arm to support policies dictated by the IMF and extracted under duress and with puny positive results for developing countries, if any. Such policies have not historically answered to the needs of the developing countries, as observed earlier, and on the contrary, have promoted the interests of a few hegemonic powers and of certain specific interests within them, to the detriment of those in need of support.

Similarly, the WTO has been, since its inception on the 1st January 1995, a very effective instrument for the promotion of the selective prosperity of a few, the rich countries, to the detriment of the many, the developing economies. Because of the dramatic modifications brought about by the Uruguay Round (1986-1994), the WTO has been more detrimental to the interests of the emerging countries than the GATT[15].

Reports made by several international bodies, such as the UN, World Bank and the IMF, put the advantages for the rich countries from the Uruguay Round, and thus the WTO structure, from 66% to 80% in their favour. Such advantages were materialised by many different agreements, such as in the General Agreement on Trade in Services (GATS), which granted access to service providers from rich countries to the markets of the developing nations, whilst allowing the economies of the first to remain closed *inter alia* by horizontal barriers.

The Agreement on Trade Related Investment Measures (TRIMs), thoroughly inspired by Milton Friedman's ideas, extensively disallowed emerging countries from pursuing measures with a view to promoting economic growth, social development and the protection of their nascent industries. The TRIMS additionally contradicted the work of other international economic agencies, such as the UN's Economic Commission for Latin America and the Caribbean.

The same is true for the Agreement on Subsidies. It is to be noted that, when of the acute phases of the financial crisis in September 2008, the rich countries did not hesitate to violate both the TRIMs and the Agreements on Subsidies in a very thorough and robust manner.

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[14] World Bank Reforming to Meet New Challenges, press release number 2010/092/exc, October 6, 2010, at HTTP://worldbank.org,

[15] Goyos Jr., Durval de Noronha, Diário da Crise, *op. cit.* page 225 *et seq.*

Developed countries disbursed in the 12 months from that date approximately 10% of the world's GDP in subsidies, most of which inconsistent with the multilateral trade order of the WTO.

The Agreement on Agriculture permits developed countries to practice subsidies which are devastating for developing economies. The agreement on trade related aspects of intellectual property (TRIPs) is absolutely redundant, in view of the existence of another international organisation, the WIPO, and was structured to favour the pharmaceutical sectors of the developed economies. The TRIPs is an obstacle for the promotion of policies of public health worldwide.

The Agreement on Dispute Resolution of the WTO does not contemplate the execution of the decisions or awards of the arbitral body and cannot be seriously regarded as a judicial structure[16]. Its conceptual failures are the frustration of many countries and its attempts at the creation of international law in derogation of the interests of developing countries truly scandalous.

In addition, similarly to what happens in other international organisations, such as the IMF and the World Bank, the state of the governance of the WTO is lamentable, not only because its leadership is given by developed countries, two thirds of the staff comes from the rich economies, but also because its workings have had very little transparency in matters of importance.

Conclusions – some scenarios.

Thus, it remains clear that there is a necessity to promote a complete overhaul of the international institutions, starting with the UN, but also involving the IMF, the World Bank and the WTO, not only with a view to promoting the ideal of Justice, but also to allow for international cooperation for the benefit of human kind.

Even if the conditions are now ripe for such a reform, resistance to it is fierce. This is so because the system, as structured and led in a dictatorial manner by the developed economies since the end of the Second World War in 1945, is of great benefit for the respective countries. The present economic crisis affecting such rich nations does not encourage them to alter that system, in spite of the notable economic

[16] See Goyos Jr., Durval de Noronha, Arbitration in the World Trade Organization, *op. cit.*, page 75 *et. seq.*

progress and social development in many developing countries, including the BRICs.

This is so because, evidently, the affluent countries do not want to let go of controlling a system in which they are the exclusive beneficiaries. However, in view of the delicate nature of their economies, it may be disinteresting for the rich countries to prevent greater international economic co-operation when financial resources from the emerging countries become necessary for their balance of payments.

Also, it seems rational that a controlled substitution of the US dollar as a reserve currency is to be much preferred by all to a sudden crash of the American tender. This, as we saw earlier, can only be achieved today within the ambit of an international organism such as the IMF.

In view of the gravity of the international economic situation as a result of a crisis that is not over, a scenario in which nothing is done is not conceivable. However, in view of the reluctance of the rich countries to share world power with the new emerging economies, the scenario in which very limited reforms are introduced to the world order is more probable.

This scenario will not prevent the recurrence of a second acute moment of the crisis resulting from the eventual crash of the US dollar, a new collapse of the international financial markets and a both profound and generalised new recession which could trigger military conflicts of a very serious nature.

If this becomes the generalised perception of developing countries in general and the BRICs, in particular, it may happen that new initiatives in regional agreements will take place, seeking to mitigate the effects of a renewed financial and economic crisis. Such initiatives may very well not be as good as a balanced, rational and just international system, but could be the only alternative available in the world today.