BRICS Academic Forum 2019

Searching for new ways of cooperation and development

BRICS Joint Financial Architecture: the New Development Bank

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The New Development Bank (NDB)

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The unfolding of the international financial crisis that started in September 2008 and the failure of the institutions responsible for global financial governance to promote the reforms discussed and approved in the Group of Twenty (G20) to give more representation to the emerging economies and the developing countries were factors that contributed to the decision of the BRICS (Brazil, Russia, India, China, and South Africa) to create **the New Development Bank (NDB)** and the stabilizing fund nominated **Contingent Reserve Arrangement (CRA)**.

These initiatives were designed in 2012 and then introduced in 2014 at the VI BRICS Summit, in the city of Fortaleza, Brazil.

The New Development Bank (NDB)

- **The NDB** was established with a capital of US$ 100 billion and was designed to be a bank focused on the financing of infrastructure and sustainable development projects, operate globally and be led only by developing countries.
- Besides, the bank was idealized to differentiate itself from post-Second World War financial institutions, in this case, the World Bank (WB) regarding the **mandate, *modus operandi* governance, and decision-making structure**.

The Creation of NDB

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- The creation of the NDB was an opportunity for closer cooperation between the BRICS countries, gave concrete form to the alliance between BRICS countries, it demonstrated dissatisfaction with global financial governance (WB and IMF) and, questioned the dollar's role in the international monetary system.

The Role of NDB

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- O *NDB* was presented as an institution created to complement the efforts of other similar banks and to respond to the need to build a modern development agenda geared towards issues of the 21st century, i.e. ***sustainable development***.
- Complementary mechanism to the efforts of multilateral and regional financial institutions of narrowing the ***infrastructure deficit* of developing countries**.
- Channeling resources applied in the financial markets to ***long-term credit***.

The Role of NDB

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Narrowing the infrastructure deficit of developing countries

TABLE 1

Infrastructure financing needs (anual)

Global investment	US$ 5 to 7 trillions
Invest. in countries in development	US$ 1 to 1,5 trillion
Invest. Asia	US$ 620 billion
Invest. Latin America and Caribbean	US$ 300 billion
Source: Unctad, 2016	

The Role of NDB

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Providing **long-term financial resources, for** investments in the real economy.
Channeling resources applied in the financial markets to ***long-term credit***

TABLE 2

Worldwide financial assets, 2015

Worldwide stock in financial assets*	**US$ 325 trillion**
Global savings (annual)	**US$ 19.5 trillion**

*** Referred to total assets held by financial corporations**

ıdow Banking Monitoring Report 2017 e World Bank Data.

The search for difference: new approaches

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- **Clear and lean mandate.** Global institution opened to UN members. A bank of projects, agile and focused on infrastructure financing and sustainable development projects.
- **Acting in partnerships,** based on relations of equality and mutual respect, paying attention to the autonomy and sovereignty of countries in establishing their internal policies and selecting projects (without conditionalities in this area).
- **Governance** with symmetry in decision-making power, equal voting power among the founding members and the first bank led by developing countries.

The search for difference: new approaches

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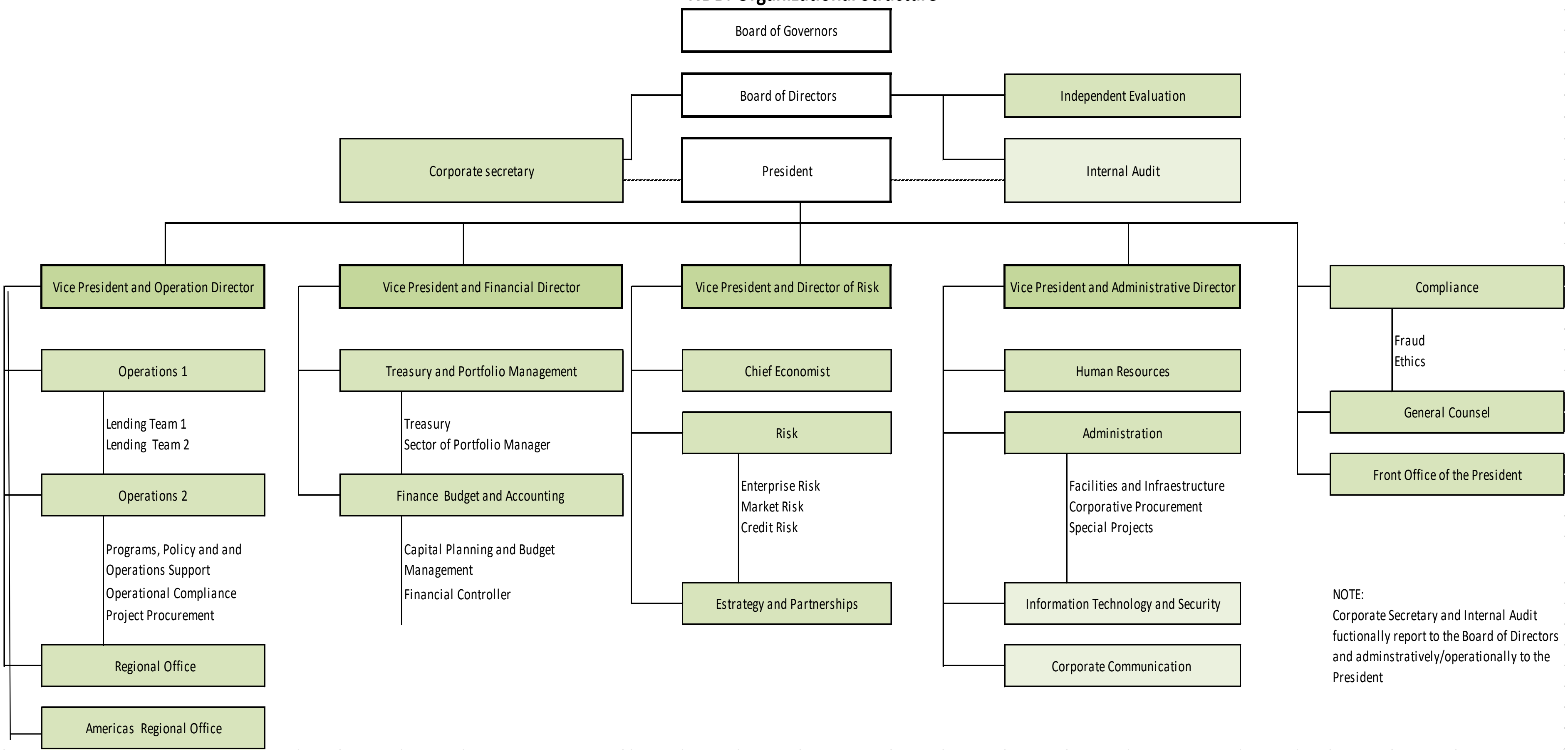
Decision-making power

- Voting power of the founding members (BRICS) is equal to each other (20%) and they jointly hold 55% of total voting power
- Developing countries can reach up to 25% of voting power, (they can take loans)
- Developed countries, which as members can contribute to capital, have a total voting power of 20% (They can not take loans)
- No single country may have more than 7% voting power (non-founding member).

NDB: Organizational Structure

Figure 1

NDB: Organizational Structure



The NDB Operation

The NDB started as a legal entity in July 2015 during the inaugural meeting of the Board of Governors held at the 17th BRICS Summit in Ufa, Russia;

In February 2016, an agreement was signed with the Government of China and a Memorandum of Understanding with the Shanghai Municipal Government to establish the seat of the bank in that city, making it operational .

That same year the institution received the first installments of resources from the BRICS countries as part of the process of paying its capital.

The NDB Operation

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"Additionalily"

- ***New Relationships.*** A relationship of equality, mutual respect and trust between NDB and member countries.
- ***New Projects and Instruments.***

- commitments in its first five years to Sustainable infrastructure development;

- Moving beyond long-term loans to include guarantees, syndicated loans with private investors, equity investments, project bonds and co-financing arrangements;

- <u>Local currency financing</u> is a key component of NDB's value proposition, as it mitigates risks faced by borrowers and supports the deepening of capital markets of member countries.

New Approaches. NDB aims to be fast, flexible and efficient, without unnecessary bureaucracy

The NDB Operation

Capital

- **authorized capital:** US$ 100 billion
- **subscribed capital:** US$ 50 billion
  - *callable capital*: US$ 40 billion
  - *paid in capital* US$ 10 billion (within seven years)

The NDB Operation

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TABLE 3

NDB: Schedule of Paid-In Capital (US$ million)

Year	Part (Annual contribuition, By country)	Total contribuition (Annual)	Accumulated
Jan 2016	200	1,000	1,000
Jan 2017	240	1,200	2,200
Jan 2018	260	1,300	3,500
Jan 2019	300	1,500	5,000
Jan 2020	350	1,500	6,500
Jan 2021	350	1,750	8,250
Jan 2022	350	1,750	10,000

Source: NDB`s General Strategy 2017-2021

The NDB Operation

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2016 to July 2019

The performance In its first three years of operation involved:

- **38 projects (US$ 10.2 bn)**;
- **Paid in Capital (US$ 5.6 bn)**
- **Project Preparation Fund**
- **AA+ international credit rating** with stable outlook (S&P Global Ratings and Fitch Ratings
- **AAA China domestic rating received (***China Chengxin Credit Rating Co*., Ltd. e *China Lianhe Credit Rating Co*., Ltd.)
- **1º RMB Green Bond Programme.** July 2016
- **1º RMB Bond Programme** registered in China. Jan. 2019
- elaboration of the general terms and conditions for the admission of new members;

The NDB Operation

- Establishment of the first regional office in Johannesburg, South Africa.
- Establishment of the first regional office in Johannesburg, South Africa.
- Signature for the establishment of the NDB Americas Regional Office in Brazil
- Approval of operational and risk policies

The NDB Operation (lending activities)

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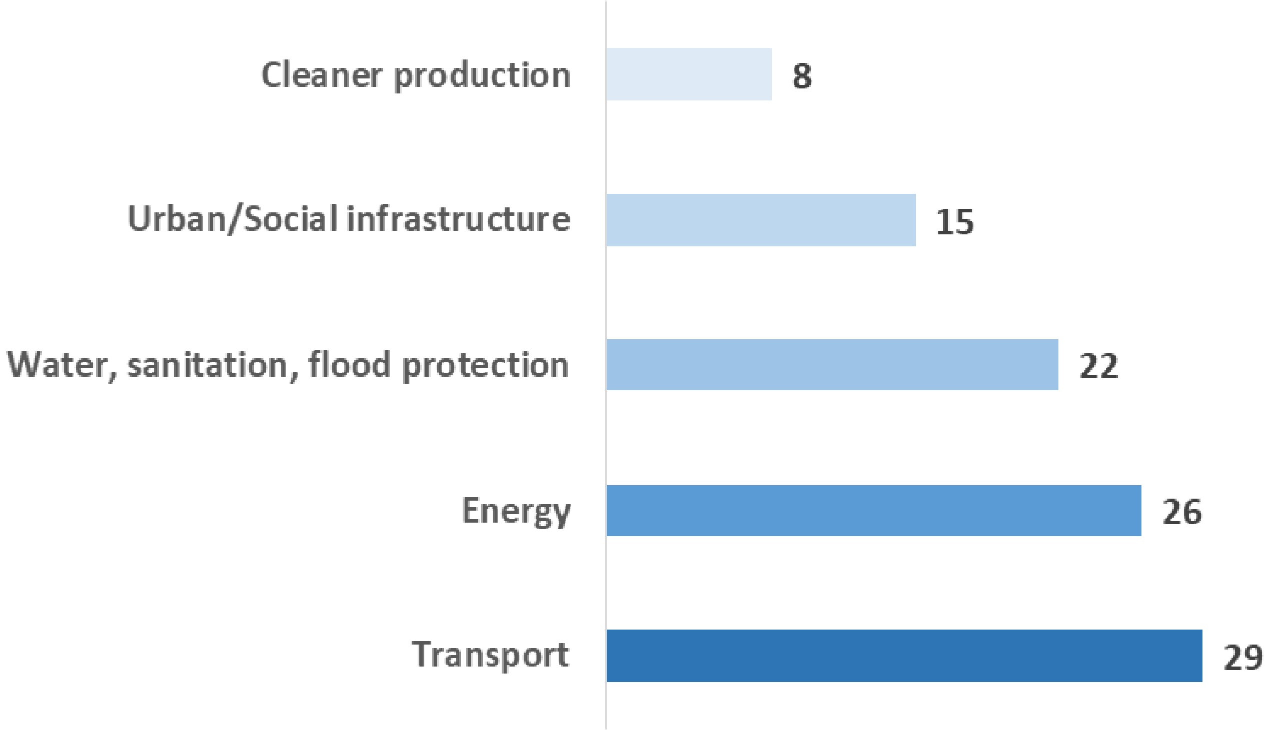
Approved loans: US$ 8,1 billion (2016-2018)

GRAPHIC 1

Loan approvals, by sector (2016-2018) (%)



Source: NDB 2019 (Investor Presentation. Jan 2019)

The NDB Operation (lending activities)

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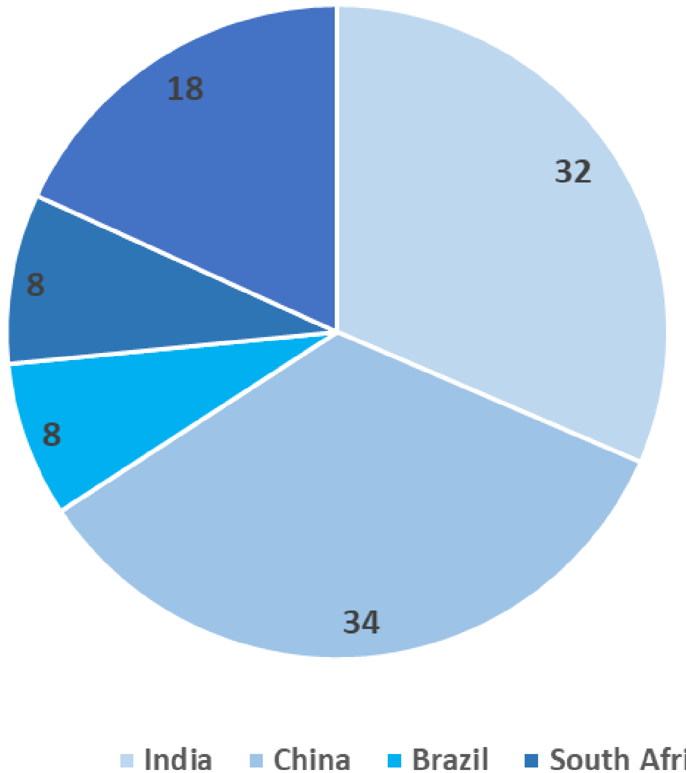
GRAPHIC 2

Participation of the five countries in the approved loan portfolio (2016-2018) (%)*



NDB:Annual average value of loans (US$ million)

China: 924
India: 850
Russia: 490
South Africa: 227
Brazil: 207

*The total value divided by three years of database operation.

Source: NDB Investor Presentation 2019

The NDB Operation (lending activities)

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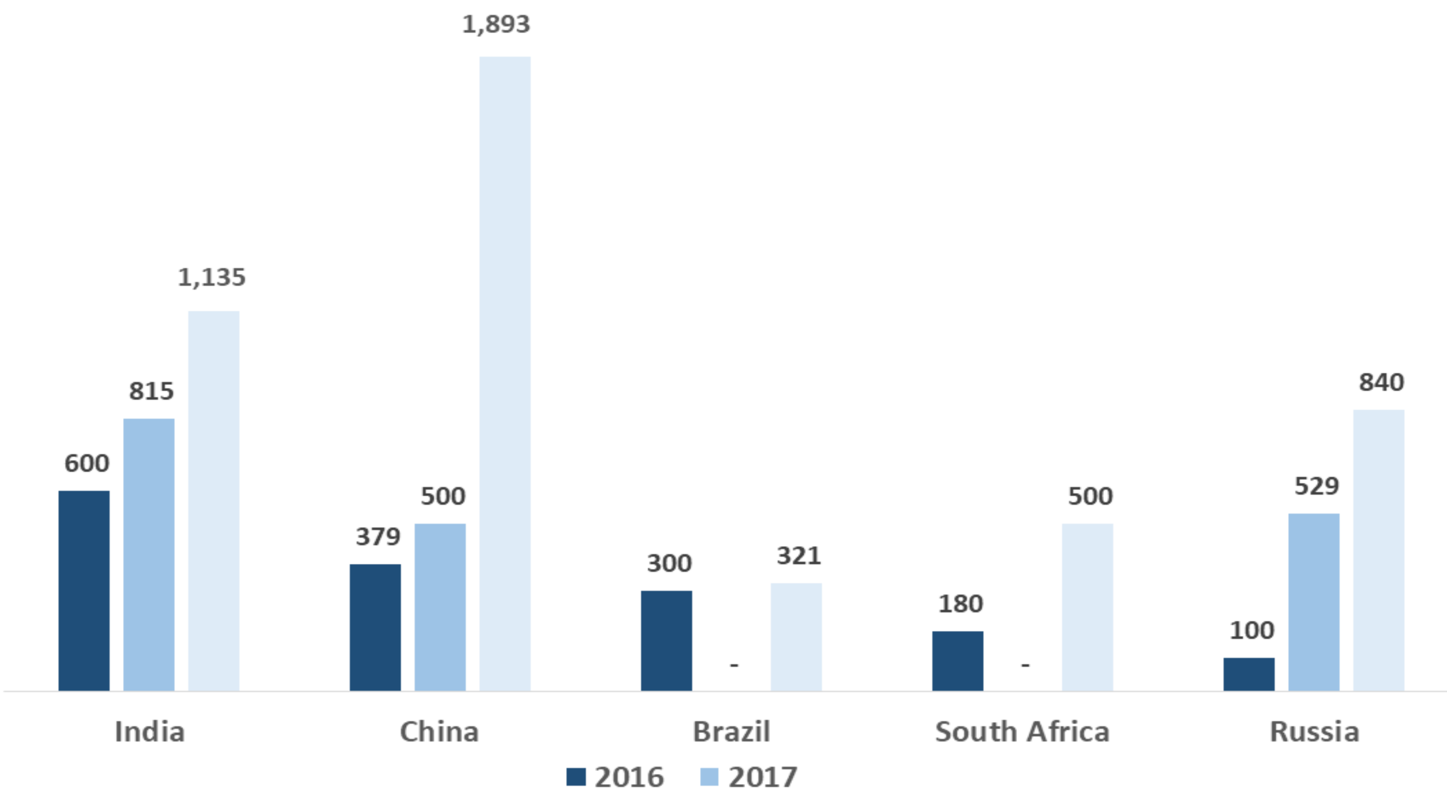
GRAPHIC 3
Loan approvals, by country (2016-2018)
(US$ million)



Source: Investor Presentation 2019

The NDB Operation as at July 15, 2019

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Loan approvals by Country, Sector and Risk

Country	Sector	Loan type (Risk)
·India 28%	·Energy 30%	·Sovereign/ Sovereign-guaranteed 85%
·China 38%	·Transport 36%	·National Financial Intermediaries 8%
·Russia 14%	·Water/Sanitation/ Flood Protection 19%	·Non-Sovereign 7%
·Brail 6%	·Urban/Social 10%	
·South Africa 14%	·Cleaner Production 5%	

China

2016 to July/2019

Part.: **37.6% in the bank's portfolio (13 projects = US$ 3,865 bn).**

Purpose: Financing of distributed solar power Project; financing of offshore wind power; enhancement of flood control; improvement of water quality; upgrade of traditional industries, to achieve energy conservation; development of sustainable infrastructure in 7 small cities; on-lending to promote sustainable economic development; upgrading urban and rural water systems; developing a green bus system.

Type: Sovereign financing (Government of China).

India

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2016 to July/2019

Part.: **27,8% in the bank's portfolio (9 projects=US$ 2,850 bn)**

Purpose: On-lending to renewable energy projects in solar and Wind energy; upgrade of 1,500 km of roads; developing the rural drinking water supply scheme in the state; construction and upgrading rural roads and bridges; construction of three metro lines;

Type: Sovereign financing (Government of India) and Sovereign-guaranteed financing.

Russia

2016 to July/2019

Part.: **14,3% in the bank's portfolio (6 project=US$ 1,468 bn).**

Purpose: Construction of small hydroeletric power plants; development of infrastructure and implementation of information technology systems; construction of a toll transport corridor; Modernisation and construction of integrated water supply and sanitation systems; development of tourism infraestructure; construction of water treatment facilities, transport andlogistics infrastructure.

Type: Loan to NFI, Sovereign financing and Non-Sovereign financing.

South Africa

2016 to July/2019

Part.: **14,2% in the bank's portfolio (6 projects=US$ 1,462 bn)***

Purpose: financing renewable energy projects; upgrading of port infrastructure to provide additional slots for larger vessels; loan to NFI for on-lendingto sustainable development projects within the energy sector; financing the construction of water transfer infrastructure; on-lending to renewable energy sub-projects; retrofitting flue-gas desulfurization equipment

Type: Sovereign-guaranteed financing, Loan to NFI and Non-Sovereign financing.

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* The country did not submit projects in 2017.

Brazil

2016 to July/2019

Part.: **6% in the bank's portfolio (4 projects=US$ 621 mn)** *

Purpose: On-lending to support renewable energy and transmission projects; improvement and reconstruction of roads and drainage, sanitation and telecommunication; upgrading of the infrastructure of 2 existing refineries;

Type: Loan to NFI, Sovereign-guaranteed financing and Non-Sovereign financing.

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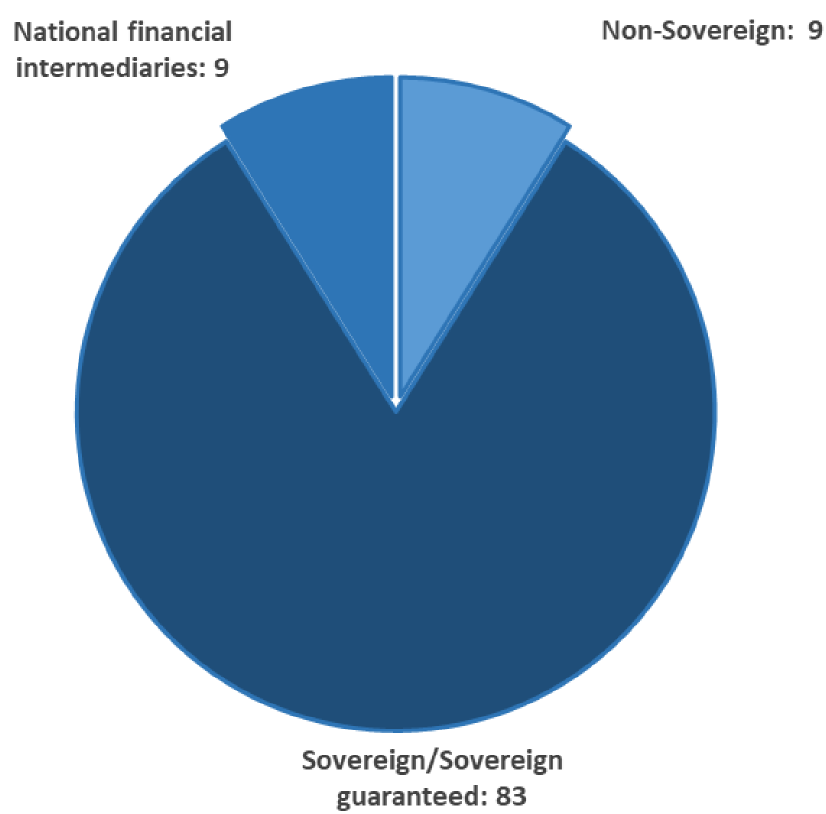
*The country did not submit projects in 2017 and there is no information about new project in the first half of 2018.

The NDB Operation (lending activities)

Most bank loans carry sovereign risk. This was a deliberate policy of the institution not to take high risks in the initial structuring of its portfolio. But in its Strategy (2017-2021) NDB states that operations with the private sector should reach greater volume in the future.

GRAPHIC 4

NDB: Loan approvals, by type of loan/risk (2016-2018)



Fonte: NDB Investor Presentation. Jan 2019.

The NDB Operation (lending activities)

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Loans / contributions (cumulative amounts, 2016-2018)

Different loan/contribution ratios that can be verified by the ratio of each dollar of loan approved by a country vis-à-vis each dollar of contribution that goes out of its budget:

- China: 4.0, meaning that this country contributed $ 700 million by 2018, earning an approval of resources four times higher than the amount paid; India: 3,6; Russia: 2,0; South Africa: 1,0; and Brazil: 0,9.

These asymmetries may change in the coming years as both countries' ability to deliver good projects and their fiscal conditions improve (which makes sovereign guarantees more difficult).

The NDB Operation (new financing instruments)

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NDB will utilize a full range of financing instruments, moving beyond long-term loans:

Guarantees, **syndicated loans with private investors, equity investments, project bonds and co-financing arrangements** with national and multilateral development finance institutions

Local currency financing is a key component of NDB's value proposition as it mitigates risks faced by borrowers and supports the deepening of capital markets of member countries.

The NDB Operation (disbursments)

- Regarding disbursements, official information available shows that between 2016-2018, only US$ 625 million was disbursed against a total of approved loans
- Disbursements / loans ratio: only **7.7%.**
- In June 2017 the bank made two projections for the approved loans and their disbursements for the period 2016-2021, one conservative and one optimistic about the evolution of the number of projects.
- Observe the following chart with the conservative projection:

The NDB Operation (disbursments)

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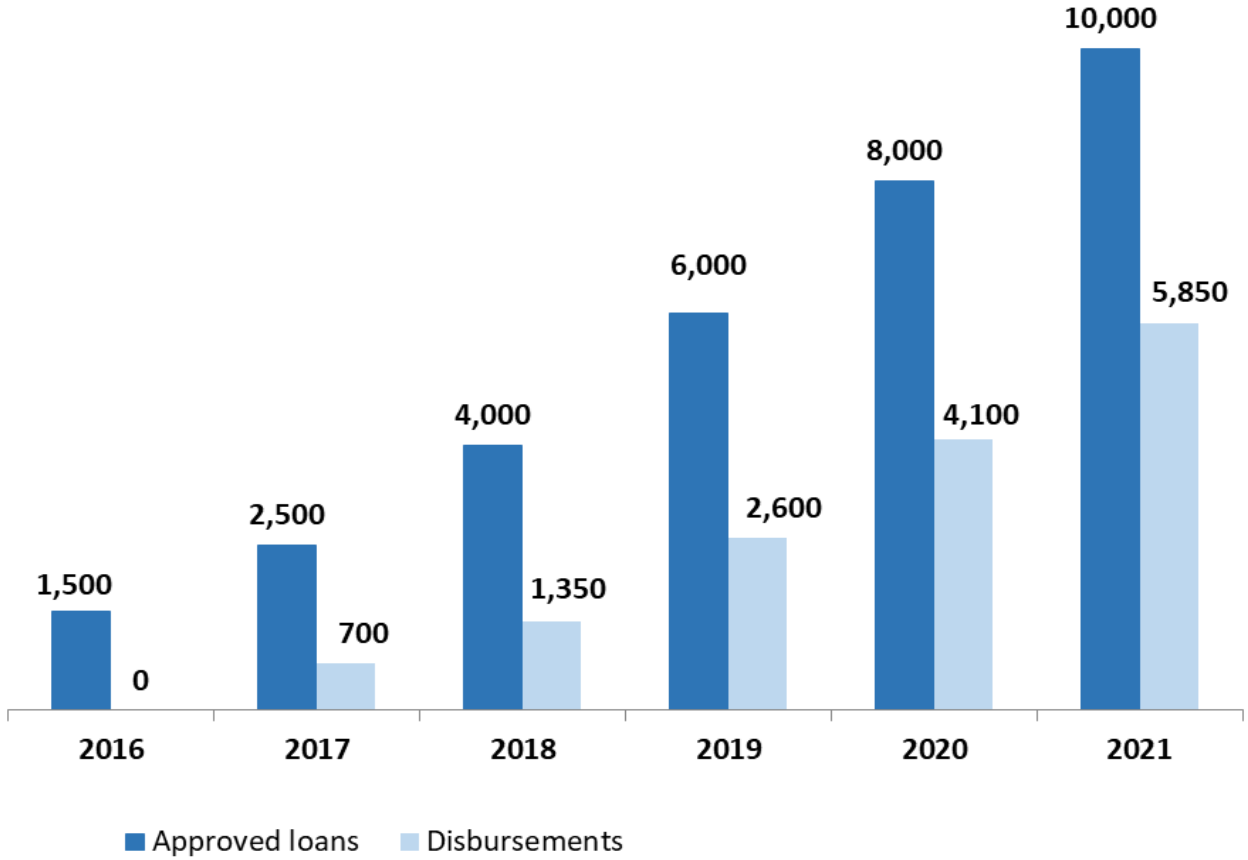
GRAPHIC 5

NDB: Projections of Approved Loans and Disbursements - conservative scenario (2016-2021) (US$ bn)



Estimated average value of each project: US$ 167 million (2017).The average loan size in both scenarios is assumed at US$ 200 million from 2018 onwards.

Source: NDB Investor Presentation. Jan 2019

The NDB Operation (disbursments)

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- In this projection, the NDB would have approved between 2016-2018 a total of 39 projects worth US$ 8 billion, and disbursed US$ 2.5 billion, ie a share of actual onlendings of **31%** of total approvals.
- However, disbursements in this period were only $ 625 million compared to a US$ 8.1 billion approval. This gives a pass-through / approval ratio of only **7.7%** over these three years of NDB operation, far below projections, even considering the conservative scenario.

For more details see:
IPEA Discussion Paper 243

Thank you!

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