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Digitalization of finance may pose a multitude of risks

Taking stock of recent developments in the digitalization of finance, the Basel Committee on Banking Supervision has warned that banks may face challenges in adopting strategies needed to remain competitive and profitable in an increasingly digital environment, and that these strategies may, in turn, exacerbate certain strategic, reputational, operational as well as system-wide risks to banks, their customers and financial stability.

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Digitalization of finance can create new vulnerabilities, amplify risks

Taking stock of recent developments in the digitalization of finance, the Basel Committee on Banking Supervision said that financial digitalization raises a number of regulatory and supervisory implications for both banks and supervisors.

by Kanaga Raja

PENANG: While the digitalization of finance can benefit both banks and their customers, it can also create new vulnerabilities and amplify existing risks to banks, their customers and financial stability, according to the Basel Committee on Banking Supervision.

In a report on the implications of the digitalization of finance for banks and supervision, the Basel Committee said that these vulnerabilities and risks include greater challenges by banks to adapt their business strategies ("strategic risk") to an increasingly digital environment, potentially heightened reputational risk to banks, a larger scope of factors that could test banks' operational resilience and operational risk, and challenges to banks' data governance.

It said there are also system-wide risks that could result from the ongoing digitalization of banking, including greater interconnection nodes across financial firms, a heightened degree of contagion in times of stress and the amplification of pro-cyclical behaviour (e.g. fire sales).

The Basel Committee underlined that advances in digitalization should not diminish the role of human judgment in risk management and supervision.

The report said that digitalization raises regulatory and supervisory implications for both banks and supervisors.

These include: monitoring evolving risks and adopting a responsible approach to innovation; safeguarding data and implementing robust risk management processes; and securing the necessary resources, staff and capabilities to assess and mitigate risks from new technologies and business models.

The latest report by the Basel Committee builds on an earlier report it published in 2018 and takes stock of recent developments in the digitalization of finance.

The report reviewed some of the key technologies across various aspects of the banking value chain, including the use by banks of application programming interfaces (API), artificial intelligence (AI) and machine learning (ML), distributed ledger technology (DLT) and cloud computing.

Such technologies are being used by a wide range of banks, albeit with varying degrees of intensity and scope, it said.

For example, it said despite the growing interest around AI/ML, most banks appear to be using such technology cautiously at this stage, especially for customer-facing services and for revenue generation.

In contrast, the Basel Committee said there has been a significant increase in the number of banks using cloud computing services in recent years, with this trend expected to continue.

The report also considered the role of new technologically enabled suppliers (e.g. big techs, fintechs and third-party service providers) and business models.

It said innovative technologies have facilitated the entry of new digital-only participants ("neobanks"), fintechs and larger technology companies ("big techs") into the provision of banking and financial services.

It said these firms often have an advantage in data and technology relative to traditional banks (e.g. digitally native platforms without legacy IT systems), and may not be subject to prudential regulation or supervision.

Advances in digitalization and financial technology ("fintech") continue to affect the landscape of the financial system, including the provision of banking services, said the report.

It said that technological

developments are disrupting the financial system through three broad channels: (i) an expansion in the set of financial services and products, as well as the distribution channels through which they are offered; (ii) the arrival of new technological suppliers of these services (e.g. big techs, fintechs and third-party service providers); and (iii) the increasing use of digital innovations for managing, mitigating and overseeing risks.

Since 2018, the digitalization of finance has continued to accelerate across a number of fronts, said the report.

Investments in fintech companies between 2019 and 2023 totalled $865 billion – more than twice the amount invested between 2013 and 2018.

Big techs, fintech firms, non-bank financial institutions and service providers are collectively playing growing roles in the provision of financial services, with increasing chains of interconnections, said the report.

"Developments in artificial intelligence and machine learning, cloud computing, distributed ledger technology, decentralized finance and various forms of cryptoassets have all raised important questions about their potential impact on banks, banking and supervision," the Basel Committee pointed out.

Potential risks

Analysing the different applications of innovative technologies and their potential benefits, the report said that for the banks, many of the opportunities afforded by new technologies relate to innovation, efficiency gains and enhanced risk management capabilities.

For consumers, digitalization holds the promise of expanding access to financial services (i.e improving financial inclusion), reducing transaction costs, improving customer experiences and increasing competition.

While digitalization can benefit both banks and their customers, it can also create new vulnerabilities and amplify existing risks to banks, their customers and financial stability, said the report.

Banks may face challenges in adopting strategies needed to remain competitive and profitable in an increasingly digital environment, it added.

Increased competition from non-bank competitors (e.g. fintechs and big techs) that offer financial services bundled with other services, together with open banking/finance regimes that facilitate portability and induce switching, may reduce banks' market share and revenues, and erode bank profitability, said the report.

In response, banks may seek to either develop their own technological capabilities, partner with new entrants to increase their digital offerings or otherwise look to diversify their revenues (e.g. through strategic partnerships with non-financial services firms such as e-commerce platforms).

These strategies may, in turn, exacerbate certain risks, the report emphasized.

It stressed that large-scale digital transformation projects carry both strategic and operational risks.

"While many banks have been increasing their technological capabilities, efforts have been impeded by problems with legacy infrastructure and a lack of staff expertise."

In this regard, the report said that smaller banks may be particularly vulnerable as they generally lack both the financial and technical resources to improve their digital capabilities.

"An inability to improve digital capabilities could put banks at a competitive disadvantage relative to more nimble, digitally native entrants."

It said bank partnerships with non-banks or other technology-focused firms may also give rise to strategic risks.

Dependencies on non-bank entities for the origination of business could leave banks vulnerable to loss of control over volumes, product design and origination processes, while remaining accountable for risks, it added.

In certain arrangements, banks may lose ownership of the customer relationship and thereby risk the possibility of non-bank partners taking their customer base elsewhere, which would result in a sudden loss of business for the bank with potentially significant implications for the bank's liquidity and financial performance, it said.

"Bank partnerships may also give rise to narrow banking models in which banks provide only a limited set of services (e.g. deposits or payments) to non-banks."

The report said this lack of diversification could create business model and balance sheet vulnerabilities, such as an over-reliance on fee income.

Banks' use of certain technologies and partnerships with non-banks or other interactions with third parties may also lead to heightened reputational risk, it pointed out.

"Reputational risk may arise from operational failures, or failures to comply with relevant laws and regulations, and can be particularly damaging for banks as the nature of their business requires maintaining the confidence of depositors, creditors and other market participants."

Banks may face reputational risk where they rely on certain models or automated processes, said the report.

For example, the use of complex AI/ML models and their lack of transparency, may increase the risk of unfair or discriminatory outputs which could lead to considerable adverse publicity as well as regulatory penalties.

It said in BaaS (banking as a service) arrangements or other interactions with third parties, issues with non-bank partners or service providers could affect the bank's business or operations, and its reputation among consumers, investors and professional service providers.

"This could potentially limit a bank's ability to, for example, obtain liquidity or professional services from external parties."

The report said even where liability is clearly assigned between a bank and third parties, banks may still face considerable reputational risk in the event of customer grievances, e.g. when customer data are compromised as banks are often viewed as the custodians of customers' data.

In response to reputational risks, banks may also face "step-in" type risks, it added.

For example, a bank may feel obliged to act to maintain continuity of service and/or to protect the values of end- users' assets in cases of financial distress with non-bank partners.

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events (including legal risk, but excluding strategic and reputational risk).

According to the Basel Committee, operational risks can manifest in a variety of different ways.

The report said that digitalization-related developments share certain common features that introduce additional complexity in the delivery of banking services, and that could exacerbate or amplify operational risks, including model risk, technology risk, cyber risk, legal uncertainty, compliance risk, fraud-related risks, and third-party risk.

For example, the report said that the use of AI/ML gives rise to potential model risks. While these may present similarly to other analytical methods, they may also amplify (or introduce novel) risks depending on the specific use case.

AI/ML approaches also have the potential to be "overfit" – that is, they hew too closely to the data on which they were trained and may not generalize to other conditions or circumstances.

The use of AI/ML can also reflect biases and inaccuracies in the data they are trained on, and potentially result in unethical outcomes, said the report.

It also said that banks' legacy IT systems may not be sufficiently adaptable, or implementation practices, such as IT change management, may be inadequate to support the use of new technologies.

The integration of new technology with legacy systems can also add additional layers of complexity, it added.

Furthermore, the report said new technologies and new business arrangements can increase cyber risks if controls do not keep pace with change.

Bank systems have multiple points of contact with outside parties, which provide potential interfaces and entry points for cyber attacks, it noted.

The report also said a heavier reliance on APIs, cloud computing and other new technologies which facilitate increased inter-connectivity with actors or sectors not subject to equivalent regulatory expectations, could make the banking system more vulnerable to cyber threats.

Digitalization can also facilitate new types of fraud, with fraudsters deploying more sophisticated techniques to target bank customers, said the Basel Committee.

It said that this can include, for example, the use of deepfakes (a type of synthetic media technology that uses AI to manipulate or generate visual and audio content that appears real) to commit account takeovers, loan fraud or wire fraud.

"More generally, operational risks may be exacerbated by poor governance and risk management practices."

Risks could be heightened where banks' governance frameworks are not modified to adapt to new technologies; there is inappropriate accountability and responsibility; a lack of technological literacy, including the inability to attract, build and retain talent; poor oversight of data governance; and use of systems and applications developed by third parties, said the report.

Effective management of operational risks is important to minimize potential operational disruptions and their impact on banks' operational resilience, it added.

The report also drew attention to data issues and related risks.

Many new technologies and applications are data intensive and leverage new data sources – or existing data in new ways – which may exacerbate banks' data governance challenges, it said.

"In particular, the volume, velocity, variety, quality and integrity of data may heighten data governance risks."

Alternative data generally means non-traditional data or data not typically used to date by banks, it noted.

For example, it can include utilities billing and payment information, as well as images, audio, video and social media information.

Alternative data raise specific risks and challenges for banks' data governance, including use of data without a long history (and whether they will continue to be predictive and explainable though the life-cycle of the data or with changing conditions); issues with privacy and consent (especially obtaining customer consent upfront); and potential bias within the data, said the report.

The use of alternative data in combination with AI/ML applications may also exacerbate bias and explainability concerns, it added.

In addition, the use of new data sources or techniques may also present challenges in integrating these processes with legacy risk management processes.

For example, the report said the use of new data to underwrite credit products may be challenging to integrate with existing credit loss modelling when assessing the adequacy of allowances for credit losses.

"Increased inter-connectivity and the sharing of data between banks and third parties creates potential challenges for data security and protection, and may introduce additional vulnerabilities as different parties access a bank's data. This may increase the possibility of data breaches and result in a larger surface area for cyber attacks."

The report said that new partnerships with non-banks may also present unique and potentially complex risks surrounding data ownership and accessibility.

For example, it said in some jurisdictions the end user in a bank-fintech arrangement may also be a customer of the bank, necessitating the bank's collection of certain information on the arrangement's end users to understand its own compliance obligations and risks even in instances where the bank does not have a direct relationship with the fintech's end users.

It said that some fintechs may differentiate between types of data, such as data about a customer and data about the customer's account, viewing some of it as proprietary and unnecessary to share with a bank that it views as a service provider.

This may, in turn, inhibit the bank's ability to fulfil its regulatory requirements (e.g. account and transaction monitoring for anti-money laundering and combating the financing of terrorism), it added.

The Basel Committee said new technologies, applications and the entry of new suppliers into financial services may also give rise to broader banking system and financial stability risks, particularly where activities may scale rapidly.

These could include: increased interconnections; regulatory arbitrage; contagion; amplification of financial risks; fragmentation risks; and concentration risks.

For instance, the Basel Committee said that the use of innovative technologies typically leads to greater inter-connectivity and more interdependencies between market players (i.e. banks, fintechs and technology firms) and market infrastructures.

It said this adds complexity and opacity, which can make it more difficult for supervisors to identify, assess and respond to risks.

Moreover, the complexity of these networks and chains of interconnection are yet to be tested in an economic downturn, the report pointed out.

It also cautioned that technological advances increasing the speed with which financial transactions can occur, coupled with the real-time transmission of information through digital channels, may increase the speed with which contagion may spread across institutions or markets.

The emergence of multiple forms

of digital money (including tokenised money), may also increase the risk of contagion to bank deposits, it added.

Digitalization-related developments may also amplify more "traditional" financial risks, said the report, adding that liquidity risks could be affected in various ways.

For example, liquidity stress may become more acute due to the speed at which deposits can be withdrawn; the use of tokenised assets could increase intra-day liquidity needs; and fintechs' reliance on banks to hold reserves or maintain operating accounts could precipitate liquidity and/or other stress on the bank's financial condition if the fintech were to fail or to leave suddenly.

The use of automated models may also encourage and amplify pro-cyclical behaviours, the report said.

Risk management

The Basel Committee noted that banks are implementing various strategies and practices to mitigate the risks.

The report pointed out that effective governance structures and risk management processes are fundamental to identifying, monitoring and mitigating risks associated with the digitalization of finance.

Banks may also mitigate specific digitalization-related risks – such as those stemming from API or AI/ML models by enhancing controls and pursuing an "across the bank" human-centric approach to overseeing the use of such technologies, it said.

Similarly, the report noted that banks manage data-related risks through robust governance arrangements and enhanced security protocols.

Banks may also reinforce their due diligence and operational risk management to mitigate the risks stemming from their reliance on third-party service providers, it said.

In practice, the Basel Committee said many of these risk mitigants are still evolving and have not yet been tested through different phases of the business cycle or periods of stress.

Regulations and supervisory frameworks have also evolved in response to the digitalization of finance, it added.

For example, it said some jurisdictions have expanded the scope of the regulatory perimeter in their legislative frameworks.

Most authorities also require new banking applications to follow the same framework applied to "traditional" bank entrants, with a few jurisdictions applying a distinct process for digital-only banks.

Many jurisdictions have also issued specific supervisory guidance related to different aspects of the digitalization of banking (e.g. on model risk management and cloud computing).

Supervisors are also reviewing and adjusting their approaches and tools to mitigate the risks from digitalization while also harnessing their benefits in a responsible manner, said the Basel Committee.

The report also outlined the regulatory and supervisory implications for both banks and banking supervisors.

It said that at a macro-structural level, supervisors should continue to monitor – and it is important for banks to mitigate – the risks stemming from the evolving nature of banking as a result of technological innovations.

"The adoption of innovative technologies and business models should be guided by a principle of responsible innovation."

It said it is important for supervisors to strike the right balance between enabling responsible innovation while also safeguarding the safety and soundness of the banking system and financial stability.

The report said as a result of the increasingly blurred lines between banks and the provision of banking services, integrating the principle of "same risk, same activity, same regulation" in regulatory and legal frameworks may help avoid regulatory arbitrage.

Highlighting the implications of specific digitalization themes, the report recognizes data as a critical resource, which necessitates a commensurate level of safeguards.

The use of service providers should be subject to robust risk management practices and processes in a risk-based and proportionate manner, it said.

More generally, advances in digitalization should not diminish the role of human judgment in risk management and supervision, the Basel Committee underlined.

The report also highlights the implications of digitalization for capacity-building and coordination.

It said that it is important for both banks and supervisors to have sufficient resources and staff with the necessary capabilities, knowledge and skills to assess and mitigate risks from new technologies and business models.

"Digitalization raises issues that go beyond the scope of prudential supervision. Accordingly, communication and coordination among bank supervisors and other relevant authorities, within and across jurisdictions, is important to address these considerations," it concluded. *(SUNS 10011)*

"Responsible consensus" proposal rejected at WTO

A proposal by Singapore and seven other countries on "responsible consensus" was rejected by many developing countries at a recent meeting of the World Trade Organisation's General Council.

by D. Ravi Kanth

GENEVA: Many developing countries, including the African Group and the ACP (African, Caribbean, and Pacific) Group on 23 May rejected the proposal on "responsible consensus" floated by Singapore along with several other countries at the World Trade Organization, said people familiar with the development.

The United States seemingly adopted an ambivalent position on consensus-based decision-making, saying that "consensus" is essential, adding that members have the option to block decisions that conflict with vital national interests, said people who took part in the meeting.

China supported both consensus-based decision-making as well as "responsible consensus", suggesting the possibility of voting when decisions on "low-hanging fruits" are blocked due to consensus-based decision- making.

At the two-day General Council meeting that continued on 23 May, its chair, Ambassador Petter Olberg of Norway, clubbed two proposals to be taken up together - one by the ACP Group on preserving consensus-based decision-making and the other on "responsible consensus" by Singapore and seven other countries, said people familiar with the discussions.

Elaborating on its stand, the US said that those blocking a decision must be willing to engage in discussion, explain their position, and provide justification for their decision, said people, who asked not to be identified.

Apparently, the US said that members should focus on how to build consensus, while recalling that during the Uruguay Round of trade negotiations between 1986 to end-1993, the US Congress instructed their negotiators to preserve consensus, said people who asked not to be quoted.

The US position on consensus at the General Council meeting on 23 May seemingly differed from its earlier stance prior to the WTO's 13th ministerial conference (MC13) in Abu Dhabi when it said that members could adopt decisions based on "responsible consensus", said people familiar with the discussions.

China said that both the ACP Group's proposal to preserve consensus-based decision-making and Singapore's proposal on "responsible consensus", "are complementary rather than contradictory."

According to China, "reflections on the practice of "decision-making by consensus" is very timely, in light of the results of MC13."

Without mentioning the setback suffered by the proponents of the Investment Facilitation for Development Agreement at MC13, China said "the inability for decision-making on even the low-hanging fruits harms every member, in particular small members, and undermines the institution itself."

China also drew attention to the possibility of voting as mentioned in the Marrakesh Agreement, suggesting that "when WTO no longer can deliver, due to abuse of consensus, another situation could also happen, i.e. "vote with the feet"."

China said while it values the consensus-based practice the most, it supports "the idea of responsible consensus, in order to preserve the consensus-based practice, and in the end, to preserve the multilateral trading system, and to benefit all members, especially small ones."

To preserve consensus-based practices, China said that three things are needed. They include "good faith", "responsibility" and "trust."

Canada is understood to have said that it is not seeking any amendment to the Marrakesh Agreement to advance "responsible consensus", said people familiar with the discussion.

In contrast to the rather ambivalent positions, Indonesia said that "the principle of consensus has long been the primary foundation of decision-making at the WTO" especially for developing countries.

"Indeed, with this mechanism, a member, regardless of its size and world trade share, will be equivalent and have equal say," Indonesia said.

"This will also ensure the balance and equity of WTO decisions."

Indonesia expressed doubts "whether it is necessary to have a separate GC [General Council] decision - that will most likely re-interpret and even transform the existing consensus principle into the so-called "responsible consensus"."

Further, it said the draft decision on "responsible consensus", "may trigger systemic implication to the existing decision-making mechanism as well as its impacts to the legitimacy of WTO decisions."

Indonesia said that it would "encourage members to show that they are being responsible - in terms of realizing their commitment - including through rebuilding trust among members and take concrete measures that will enable for more progress on key issues based on previous Ministerial mandates."

ACP proposal

In a communication (WT/GC/W/932) circulated on 7 May, titled "Preserving the Current Practice of Consensus- based Decision-making in the WTO," the ACP Group argued against any departure from the existing practice of consensus-based decision-making at the WTO that provides "equity" to all Members.

In its statement at the meeting, the ACP Group underscored the need for WTO members to deliver more across a wide range of areas, some of them long-standing, as is the case with agriculture and even fisheries subsidies.

However, it noted that the WTO is being weighed down by geopolitical fissures, lack of trust amongst and between Members, and frankly, different visions about what kind of WTO Members want, said people familiar with the discussions.

It emphatically said that its members do not share the view that introducing qualifiers to the consensus principle is the way in which to improve outcomes in the WTO, said people familiar with the development.

The ACP Group reaffirmed Article IX, paragraph 1 of the Marrakesh Agreement establishing the WTO, which states that "The WTO shall continue the practice of decision-making by consensus ..."

It noted that the Marrakesh Agreement is void of qualifiers for this consensus principle.

It said that attempts to introduce qualifiers such as "responsible", "flexible" and "constructive", could lead to unintended consequences, including the disenfranchisement of some Members from their treaty-embedded right to contribute to decision-making in an inclusive and equitable manner.

Further, attempts to bring qualifiers now or in the future carry grave systemic risks, chiefly for developing Members, the ACP Group argued.

The ACP Group suggested that there would be the risk of collateral damage should certain qualifiers be introduced to further clarify the meaning of consensus.

It gave an example that while the concept of "responsible consensus" seems innocuous enough, there is a possibility that there are some Members who may want to go much further than this and therefore open the door to change fundamentally the WTO's decision-making arrangements.

It emphasized that among multilateral organizations, the WTO is unique in terms of how it makes decisions, as compared to the United Nations where the P5 Members (of the UN Security Council) are able to exercise their veto power which represents the perpetuation of a system which emerged after the Second World War.

More importantly, the consensus-based decision-making at the WTO acts as a buffer against inequity and power, the ACP Group said.

It emphasized the need to preserve the current practice of decision-making by consensus.

Several developing countries, including South Africa, strongly supported the ACP Group proposal.

On behalf of the African Group, which is a co-sponsor of the ACP Group proposal, Chad said that the utility of the Marrakesh Agreement establishing the WTO lies in large part in its core foundational principle of decision-making by consensus and an equal voice for all Members regardless of might or size.

According to Chad, the principle and practice of decision-making by consensus does not only ensure equal rights, but also ensures that all Members, big and small, have an equal chance at agenda-setting, including outcomes that are inclusive of their issues of priority, said people familiar with the discussions.

The African Group, said Chad, is not in a position to support any qualifiers to the foundational principle of the WTO, as contained in the proposed draft decision on "Responsible Consensus".

It raised several questions such as:

1. What is the added value of a General Council decision on "responsible consensus" and how will it work in practice?

2. How will the General Council Decision enable members to concretely adopt a win-win approach in WTO negotiations?

3. How exactly will the qualifiers introduced in the document, such as "responsible" consensus, "flexibility", address power dynamics, imbalances in approaches and the prioritization of issues before Members, in particular those of particular interest to developing Members?

4. What is the document trying to address since Article IX of the Marrakech Accord also provides an alternative in the absence of consensus?

"Responsible consensus"

The proposal (WT/GC/W/933) on "responsible consensus" was co-sponsored by Costa Rica, The Gambia, Korea, Norway, Peru, Singapore, Switzerland, and Chinese Taipei.

The co-sponsors made a strong case for "responsible consensus", urging members "to uphold the practice of consensus in a responsible manner in order to ensure that the WTO remains as the cornerstone of the rules-based multilateral trading system, and maintains its relevance by delivering shared prosperity for all its Members."

Several industrialized countries supported the proposal on "responsible consensus", but it failed to attract support and traction, said people who asked not to be quoted.

"Significantly, the rejection of the demand for responsible consensus at the General Council meeting almost made the proposed retreat on 8-9 July redundant", said a person who asked not to be identified. *(SUNS 10013)*

GC chair convenes retreat to make WTO a "forward-looking" body

The chair of the World Trade Organization's General Council (GC) has proposed that a retreat be held on 8-9 July whose underlying goal is to ensure that the WTO remains a "forward-lookingt" organization.

by D. Ravi Kanth

GENEVA: The World Trade Organization's General Council (GC) chair on 22 May informed members that a retreat will be convened on 8-9 July to discuss how the WTO can remain a "forward-looking organization" amidst continued stalemates on several issues, said people familiar with the development.

The "hidden" goal of the retreat appears to be to change the principle of consensus-based decision-making as enshrined in the Marrakesh Agreement that established the WTO in 1995, said a trade envoy, who asked not to be quoted.

Ahead of the GC chair's proposed retreat on 8-9 July, another retreat will be convened on 2-3 July to discuss the way forward in agriculture, said people familiar with the development.

Although the exact venues for these two retreats are yet to be finalized, it appears that they might take place at the WTO's headquarters, said a person who asked not to be quoted.

During the WTO's General Council meeting on 22 May, the chair of the General Council, Ambassador Petter Olberg of Norway, said that the proposed retreat on 8-9 July would reflect on how work is carried out in Geneva, how Ministerial Conferences can be optimized, and how the ongoing work can be carried forward in the various workstreams.

The GC chair is understood to have said at the meeting that the underlying goal of the proposed retreat is to "ensure the WTO remains a forward-looking Organization – mindful of the pending, long overdue workstreams that require our attention and breakthrough of longstanding stalemates".

He told members that he would elicit their views on the actual content of the retreat in the next couple of weeks.

Earlier, Singapore, one of the key members of the "Friends of the System" group, proposed a retreat to discuss how to make ministerial conferences more optimal, efficient, and result-oriented following the failure of the WTO's 13th ministerial conference (MC13) in Abu Dhabi, said people familiar with the development.

As reported in the SUNS, several members, including the United States, supported Singapore's proposal.

Singapore's controversial proposal on "responsible consensus", which is being co-sponsored by several countries, including Norway, is expected to come up for discussion at the General Council meeting on 23 May, said people familiar with the development.

"July package"

At the General Council meeting on 22 May, the WTO Director-General, Ms Ngozi Okonjo-Iweala, appears to have indicated some elements of a package of deliverables at the July meeting before the summer break, despite substantial differences on issues like fisheries subsidies, said people after the General Council meeting.

In her statement as the chair of the Doha Trade Negotiations Committee (TNC), the DG said four priorities for action repeatedly came up in her recent consultations with members - fisheries subsidies, agriculture, dispute settlement reform, and investment facilitation for development, according to the statement posted on the WTO website.

On fisheries subsidies, Ms Okonjo-Iweala noted that members were "very close" to completing the "second wave" of negotiations on fisheries subsidies at MC13 and that "there is much regret that it did not happen".

"Given this, members said we must get this done as soon as possible. So, this is a top priority, and we are going to have to work very hard to complete" before the WTO's summer break, the goal indicated by many members, she added.

Echoing similar expressions, China said that it "supports to advance the negotiations on this basis and try our utmost efforts to conclude it by July."

However, several countries cautioned the DG not to rush into any deliverables, particularly on fisheries subsidies, in the face of sharp differences.

Indonesia, for example, said that it is against any attempt "aimed at making early harvest - especially without resolving our remaining concern regarding the balance of the text."

Indonesia said that it "looks forward for continued negotiations to achieve a comprehensive fisheries agreement as mandated in MC12."

On dispute settlement reform, China said that "restoring the well-functioning dispute settlement system by the end of this year is obviously the most urgent one."

Since the process has been formalized after the appointment of a new facilitator, China said "now is the time for intensive negotiations, to find solutions to the targeted issues by July."

"This is the prerequisite for reaching an agreement within 2024," China said.

Members broadly discussed five issues at the General Council meeting.

They include: (1) the report of the Committee on Budget, Finance and Administration; (2) the report of the chairperson of the Trade Negotiations Committee and report by the Director-General, who apparently drove home the message for an outcome on fisheries subsidies in July; (3) report by the General Council chair on "follow-up to outcomes of MC13"; (4) Brazil's proposal to start informal outreach meetings on agriculture, which received a mixed response; and (5) the unfinished discussion on "policy space for industrial development" by the African Group, which the US seemingly extended.

Brazil's proposal to elevate the discussions on agriculture to the General Council, instead of the Doha negotiating body on agriculture, apparently received a mixed response, with major industrialized countries and some South American countries indicating their willingness to hold informal discussions.

Commenting on the Brazilian proposal on how to move the agriculture negotiations forward, China said that "taking into account the current situation and the multiple challenges facing members, especially the developing members, we call on members to kick off frank and effective dialogues, to mull on the way forward in a creative, practical and constructive way, rather than to repeat previous failures."

China also cautioned that "the position-repeating approach will not lead agriculture to the successful outcome."

"The world has changed ... We have to think in a new way and find out new approaches. Long-standing issues, food security, responses to climate change and so on, they all need us to find solutions."

The DG welcomed Brazil's proposal, suggesting that she is confident that an outcome on agriculture is possible following the Brazilian initiative, said people familiar with the development.

On the other hand, the African Group and several developing countries expressed sharp concerns, including on the danger of compromising the discussions in the Doha negotiating body on agriculture, said people who asked not to be quoted.

Indonesia, on behalf of the Group of 33 (G33) developing countries, said that "we believe that our efforts going forward must be geared towards strengthening the Committee on Agriculture Special Session (CoASS) - rather than undermining it."

"As such, we affirm our strong preference for undertaking all negotiations within the CoASS as the mandated negotiating body of the WTO Agriculture Committee," Indonesia said.

It added that members "must level the playing field between Members in agriculture trade and correct the historical imbalances in the Agreement on Agriculture, which have long favoured a few privileged Members."

Responding to the concerns, Brazil is understood to have said that the initiative to elevate the discussions on agriculture to the General Council and the proposed informal meetings are unlikely to duplicate work being carried out at the CoASS, said people who asked not to be quoted.

To recall, the Brazilian proposal sought a decision on "moving the agriculture negotiations forward" to be adopted at the General Council in July before the summer break.

The proposal suggested some significant changes in arriving at modalities in all areas, particularly on domestic support, before the WTO's 14th ministerial conference (MC14).

NFIDCs

Meanwhile, in a related issue concerning agriculture, on the decision on net food-importing developing countries (NFIDCs), Costa Rica and Paraguay are seeking a change in the decision reached at Marrakesh, said people familiar with the development.

In a "decision by the Committee on Agriculture at its meeting on 21 November 1995 relating to the establishment of a list of WTO net food-importing developing countries for the purpose of the Marrakesh Ministerial Decision on measures concerning the possible negative effects of the reform program on the least-developed and net-food importing developing countries", it was explicitly agreed in the Marrakesh Agreement that "the following countries shall be listed as beneficiaries in respect of the measures provided for within the framework of the Decision: (a) least developed countries as recognized by the Economic and Social Council of the United Nations; plus (b) any developing country Member of the WTO which was a net importer of basic foodstuffs in any three years of the most recent five-year period for which data are available and which notifies the Committee of its decision to be listed as a Net Food-Importing Developing Country for the purposes of the Decision."

Further, the decision stated that, "Notifications under paragraph 1(b) above should be accompanied by relevant statistical data in respect of total and net imports, on a value and quantity basis, and of their relative importance as a proportion of domestic consumption of the products concerned. Such notifications should be made at least 15 days prior to the regular March meeting of the Committee in any year."

Lastly, the decision makes clear that "the Committee shall establish a list of Net Food-Importing Developing Country Members on the basis of these notifications. This list shall be reviewed by the Committee at its regular March meetings."

In an alleged move to undermine this decision, which only a ministerial conference can change, Costa Rica and Paraguay want certain countries to be removed from the list, said people familiar with the development.

Apparently, NFIDCs like Egypt, Jamaica, and Peru severely opposed any attempt to undermine the Marrakesh decision, said people familiar with the development. *(SUNS 10012)*

WTO Secretariat needs more women from developing countries

An annual report on diversity in the World Trade Organization's Secretariat issued by the global trade body appears to have failed to address the low levels of staff representation of women from developing countries in the secretariat.

by D. Ravi Kanth

GENEVA: The World Trade Organization on 17 May issued its "annual report on diversity in the WTO Secretariat" to highlight the measures it has adopted in response to a Joint Statement issued by a group of developing countries almost 14 years ago, but the report seemingly fails to address the low levels of staff representation of women from developing countries, said people familiar with the report.

Even in the case of promotions, women from the trans-Atlantic countries seem to be given priority as compared to women from developing and least-developed countries (LDCs), said people who asked not to be identified.

The report also failed to address the concerns raised by India back in 2020 on WTO staff representation from developing countries (see below), said people who asked not to be quoted.

In a restricted report (WT/BFA/W/673) issued on 17 May, seen by the SUNS, the annual report on diversity in the WTO Secretariat for 2023 provided a set of measures adopted/implemented "in response to measures proposed in a Joint Statement by Brazil, China, Ecuador, Egypt, India, Pakistan, and South Africa" in 2010.

The Joint Statement by the seven countries in 2010 raised the following points:

1. A Strengthened Diversification Policy: This could be achieved by revising the Staff Regulation with more elaborated language on diversification or by formulating a separate statement or policy paper on diversification to be approved by the General Council. The language could be closely aligned with the UN Organizations, World Bank, IMF, ITC, etc.

2. An Enhanced Recruitment with Diversification: This could be achieved by inserting in future recruitment notices a clear-cut language to give preference to candidates from under/non-represented members subject to their meeting eligibility criteria.

3. An Improved Outreach to Potential Candidates: This could be achieved by adding new dimension to existing activities of the WTO, particularly the TRTA (trade-related technical assistance) activities such as Trade Policy Courses, Regional and National Workshops, Public Forum and Geneva Week to further improve the dissemination of relevant information and reach out to potential candidates, particularly those from under/non- represented Members.

4. A Regular Review of the Situation and Discussion on Way Forward: This could be achieved with a regular review based on the annual report by the Secretariat on diversity as contained in DG's 2010-2011 biennium budget proposals and subsequent discussion among Members on the way forward. CBFA should report such reviews and discussions and possible measures to be taken to the General Council.

In response to the above issues, the WTO maintained that "following the appointment of a new Diversity, Equity, and Inclusion (DEI) Officer in March 2024, some changes have been introduced to the report with a view to provide a more comprehensive picture on the status of diversity, equity and inclusion in the WTO Secretariat."

"Like previous reports," it said that "the 2023 Annual Report provides detailed data on the composition of the WTO workforce as at 31 December 2023 by gender and geography, as well as its evolution since 1995."

The report highlighted "new insights into diversity in recruitment, showing gender and geographic statistics at each step of the recruitment process and highlighting possible measures to make existing processes more equitable and inclusive."

Further, it said "as a new feature, the report looks at how diversity translates into the two types of promotion opportunities available at the WTO and the measures that will be introduced to ensure that merit and diversity are mutually reinforcing."

The WTO said that "the report showcases a number of initiatives under consideration to support a more diverse, equitable and inclusive WTO Secretariat."

Diversity, equity, inclusion

The report contends that "diversity is key to an international organization like the WTO, whose Secretariat should represent the diversity of its membership and the people it serves."

It argues that "a diverse workforce helps facilitate better collaboration and understanding between Members with different legal systems and cultural negotiation styles."

According to the report, "diversity is also known to foster creativity and innovation, which are critical to address challenges facing global trade such as digital trade and environmental sustainability."

The report argued that "diversity needs to be accompanied by equity and inclusion strategies, in order to address systemic barriers and create a level playing field in an organization where everyone feels valued."

It said "equity recognizes that people - like Members - start from different positions and ensures that everyone has access to the same opportunities."

However, in the absence of a level-playing field given the historical disparities between the developed countries and some developing countries on the one side, and a large majority of developing and least-developed countries on the other, some specific policies akin to positive affirmation may be needed, said people who asked not to be quoted.

The report suggested that "inclusion goes beyond representation to make sure that diverse voices are heard, respected and integrated into decision-making processes such as international trade negotiations."

It argued that "like many modern organizations, the WTO was created at a time when Western men were predominant in the workforce. Its demographic make-up therefore tends to reflect this historical legacy, which requires time and intentional actions to durably transform."

Therefore, it said that "improving DEI (diversity, equity, and inclusion)" is a "key strategic priority of the WTO Secretariat."

"The Secretariat seeks to build an organization that is representative, in terms of staffing, of the Members it serves and in which gender equality, diversity, equity and inclusion principles are front and centre in decision making," the report claimed.

According to the report, "women account for 55.6% of WTO staff overall, outnumbering men by 360 to 288."

"However, as a general pattern, the higher the grade, the fewer women there are," the report said.

Figures provided in Annex 11 of the report suggest that "among professional staff, women represented 48.8% in 2023 (compared to 31% in 1995). Among the support staff, women represented 67.5% in 2023 (compared to 72.2% in 1995)."

The report, however, did not explain why women staff from developing countries and LDCs are seemingly given a raw deal when it comes to promotion to the middle and higher levels, said a person from the Secretariat who asked not to be quoted.

Staff representation

Not long ago, India made a detailed statement calling for appropriate measures to be taken to increase the number of staff from the country in the Secretariat, as its staff representation has remained stagnant in the past 25 years.

India argued that "the staff representation of many members, including India, has remained stagnant in the past 25 years. For instance, India's share in the total WTO staff in 1995 was 2.2 percent and now it is 2.1 percent."

"Almost no change! In the professional staff category, it has in fact gone down from 4.1 percent in 1995 to 3.5 percent in 2019," India pointed out in a statement made at a meeting of the WTO's Committee on Budget, Finance and Administration (CBFA).

India said, "It is not that there is not enough interest among Indians or other developing country candidates to work at the secretariat. In fact, in 2019, the highest number of applicants, across staff categories, were from India."

India pointed out that just five countries - constituting only 3 percent of the membership - account for nearly 50 percent of the total staff strength, adding that "not surprisingly", these are all developed country members.

"Therefore, we call upon more measures and active efforts to increase the diversity of the secretariat. We will work with the secretariat to achieve the diversity that the WTO truly deserves," it added.

Significantly, developing countries and LDCs that account for more than three-quarters of the WTO membership account for only 30 percent of the staff.

On the other hand, the developed countries, constituting less than one quarter of the WTO membership, account for 70 per cent of the staff.

"It is clearly evident that select developed countries continue to enjoy some kind of special and differential treatment (S&DT) in recruitment at the WTO, but often the narrative is to accuse and defame the developing countries for their legitimate S&DT entitlements in WTO agreements," India argued.

While it may be true that diversity is a sine qua non for fostering creativity and innovation in global trade, the real challenge facing the WTO at this juncture is to find its raison d'etre to "stay afloat" amidst the poly-crises that seem to tear apart the multilateral trading system and the WTO itself, said people who asked not to be quoted.

The WTO is being rapidly challenged by the two trans-Atlantic giants that created it in 1995 at the conclusion of the Uruguay Round of trade negotiations, said people who asked not to be quoted.

At a time when some WTO members are allegedly making efforts to undermine the Marrakesh Agreement, particularly the cardinal principle of consensus-based decision-making, it is imperative to ensure that the WTO remains wedded to its original principles, said people who asked not to be quoted. *(SUNS 10011)*

WTO hits CHF 4.8 million surplus, despite DG's call for budget hike

Despite calls by the Director-General for a hike in the World Trade Organization's budget, the global trade body recorded a budgetary surplus of CHF 4.8 million for 2023.

by D. Ravi Kanth

GENEVA: Despite repeated calls for hiking the World Trade Organization's budget during 2022 and 2023, the WTO Director-General, Ms Ngozi Okonjo-Iweala, on 29 April admitted that "the organization will have a budgetary surplus of CHF 4.8 million (close to USD 5 million)" for 2023, an increase that prompted her to seek "stepping up our recruitment to hire the very best staff."

In a restricted letter (JOB/BFA/102) sent to the new chair of the WTO's Committee on Budget, Finance, and Administration (CBFA) on 29 April, the DG wrote that the very best staff will be hired "utilizing the strategic staffing competency and mapping frameworks that we are developing."

It may be recalled that since she took over the reins at the WTO on 1 March 2021, the DG has embarked on reforming the WTO Secretariat based on a report prepared by the management consulting firm McKinsey & Company.

The controversial reform process generated considerable turmoil in the organization, said several people familiar with the reform-related development.

Against this backdrop, in her letter, seen by the SUNS, the DG told the CBFA chair, Ambassador Jose R. Sanchez-Fung of the Dominican Republic, "I am reaching out to you at this time because we have closed the books for 2023, and our External Auditors are in the process of auditing our Financial Statement. That statement and the audit report will be provided to Members for discussion at the July CBFA meeting."

The DG said that "before the audited statements are released to us and to Members," she wanted "to provide some informal insight to you as to our budgetary result for 2023. I do so in the interest of making sure that you and our Members have pertinent information as quickly as possible."

She said, "As we could begin to see in the 3rd Quarter Report issued to Members last year, the Organization will have a budgetary surplus of CHF 4.8 million for 2023."

Ms Okonjo-Iweala admitted that "it may seem counter-intuitive that we had a budget surplus in 2023 at the same time that we were asking for an increase in budget for the 2024 and 2025 biennium."

Behind this development, she said, "last year, we were facing considerable uncertainty as to whether Members would provide us with a budget increase as we faced inflationary pressures as well as certain unavoidable mandatory and essential expenses."

She said, "I am gratified that Members granted us a modest increase, but that decision was not made until mid-December."

The DG maintained that "we have seen a record number of Members in arrears or quite tardy in making the required contributions."

Ms Okonjo-Iweala said that "we were forced, in the interest of sound financial management, to defer necessary expenditures, to the extent we could, until this year because we did not know if we could afford to take on those longer-term liabilities."

The DG claimed that "the lion's share of the surplus is due to the record number of vacant posts that we felt was prudent to maintain so we could avoid making staffing commitments that could not be supported by our available resources in the coming biennium given that Members had not made the final decision on our budget."

Further, "related to this point are the delays in the recruitment process that we faced and the turnover in key Director and Human Resources positions, which are now being addressed," she said.

Though the DG acknowledged that "we are seeing the highest level ever of staff who have left the WTO, especially voluntary (i.e., non-retirement) departures," she did not provide any reasons as to why the "highest level ever of staff" left the organization.

It appears that several directors left the organization out of frustration and resentment over her alleged personnel policies that seemingly undermined independence and impartiality at the highest level, said a staffer, who asked not to be quoted.

Ms Okonjo-Iweala told the CBFA chair that "the large number of vacant posts has caused us to rely disproportionately on short-term staff, which cost less," suggesting that "we are affirmatively addressing this disparity."

The DG acknowledged that "the increase in voluntary departures is of concern, as is the increase in external applicants who are declining offers of employment."

Besides, she cited "two underlying problems, based on feedback we have received."

The first problem, according to the DG, is that "the WTO grade structure is lower than that of comparable international organizations."

Consequently, "prospective staff members are understandably reluctant to accept a position with the WTO that they perceive as a lateral move or sometimes, a reduction in grade level," she said.

"At the same time, staff already at the WTO are being offered positions in other organizations that are, at times, two or three grades higher," she argued, pointing out that "a related problem is that the more attractive packages (salaries and benefits) that were once a sales point of the WTO are no longer on offer. Both of these factors help to explain why staff are leaving and prospective staff are declining offers."

In conclusion, she said, since "the Members have graciously increased our budget for the 2024-2025 biennium, we have considerably more certainty to plan and spend our resources in 2024 in the manner that we set forth in our final budget request last year."

"To that end, we are committed to stepping up our recruitment to hire the very best staff within the ceiling set by Members, utilizing the strategic staffing competency and mapping frameworks that we are developing," she maintained.

She said that she wants to "undertake the essential security, information technology, and infrastructure projects that we detailed to Members last year."

In her letter to the CBFA chair, the DG said that she will "provide a recommendation to you and the Members under Financial Regulation 23 as to how to utilize the surplus, for your consideration and decision."

Modest budget rise for 2024

Last year, members approved a modest hike of 3.6 percent in the WTO's regular budget, from CHF 197.2 million in 2023 to approximately CHF 204.29 million in 2024, after rejecting a separate proposal for increased contribution to the WTO Pension Fund of CHF 4.4 million (around USD 4.5 million).

The proposed increased contribution to the WTO Pension Fund was turned down by India, Indonesia, and the Russian Federation until the WTO Secretariat carried out substantial reforms, said people familiar with the development.

The WTO budget proposal was worked out by the European Union, said people familiar with the development.

The meagre hike in the WTO's budget is a setback of sorts for the DG, who had asked for a "modest budget increase of CHF 14.56 million (around $15 million) for 2024", and an additional CHF 1.94 million for 2025, said people familiar with the development.

As previously reported in the SUNS late last year, despite the near rejection of her first budget-hike proposal in 2022, DG chose to come back again with a new 43-page proposal, which came up for a first reading at the CBFA on 18 July 2023.

Nigeria, Cameroon on behalf of the African Group, Singapore, and Switzerland among others seem to have supported the DG's proposal seeking a 7.4 percent budget hike for 2024, from CHF 197.2 million in 2023 to CHF 211.76 million in 2024, and a 0.9 percent increase in 2025, i.e., from CHF 211.76 million in 2024 to CHF 213.70 million in 2025.

But several other countries including India, Bangladesh, Nepal, the United States, and some South American countries had raised numerous questions on the need for a budget hike at this current juncture when nations are continuing to face grim economic problems, said people familiar with the discussions.

However, several EU members changed their positions from a complete rejection of an increase in the WTO budget to a meagre increase, as proposed in their proposal (Job/BFA/95), seen by the SUNS.

The big contributors to the WTO's budget like Germany, the Netherlands, and Sweden among others, who had rejected the DG's budget hike proposal for 2023, seemed to have changed their positions, said people familiar with the discussions.

The United States, given its overall share in international trade both in goods and services, will have to pay CHF 23.70 million in 2024 as compared to its contribution of CHF 22.80 million in 2023.

China, according to the EU's proposal, will be required to pay CHF 23.20 million in 2024 as compared to CHF 21.03 million in 2023.

Germany would be required to pay CHF 14.84 million in 2024, as compared to CHF 14.06 million in 2023.

Japan, which contributed CHF 7.4 million in 2023, will be required to pay CHF 7.6 million in 2024.

India's contribution will go up by almost CHF 400,000 in 2024, from CHF 4.57 million to CHF 4.96 million, while Malaysia's contribution will go up by about CHF 100,000, from CHF 1.83 million in 2023 to CHF 1.927 million in 2024, according to the EU's proposal.

As reported in the SUNS, privately, several members had cast doubts on the DG's proposal, saying that some of her allegedly lavish expenditures on her travels with a big Secretariat team of officials and expenditure for convening the Joint Statement Initiatives, which were not approved multilaterally by members, as well as the expenses incurred for the transformation exercise at the WTO Secretariat, with a nearly one million Swiss franc payment to McKinsey and Company, appeared to contribute to the crunch.

"If she is carefully managing the Secretariat, we will not be in this crisis," said a Secretariat official, who asked not to be identified. "Asking for more money to promote over 60 people a year is absurd," the official said. *(SUNS 9998)*

Putting the Third World First

A Life of Speaking Out for the Global South

Martin Khor in conversation with Tom Kruse

Cross-border bank claims fell by $377 billion in Q4 2023, says BIS

The Bank for International Settlements (BIS) has reported that while cross-border bank claims fell by $377 billion in the fourth quarter of 2023, cross-border credit, however, grew by $319 billion in the same quarter, driven by lending to non-banks.

by Kanaga Raja

PENANG: Cross-border bank claims fell by $377 billion in Q4 2023, as banks in several advanced economies (AEs) reported lower derivatives claims on the United Kingdom, a centre for derivatives clearing, according to the Bank for International Settlements (BIS).

In its latest statistics on international banking activity at end-December 2023, BIS said cross-border credit (i.e. loans plus holdings of debt securities), however, grew by $319 billion in Q4, driven by lending to non-banks.

Banks in Japan reported higher claims on the non-financial sector in the United States, it added.

BIS said cross-border dollar credit recovered in 2023, after having declined during the Federal Reserve's policy tightening and dollar appreciation in 2022.

Credit to emerging market and developing economies (EMDEs) increased by $30 billion in Q4 2023, mostly driven by an expansion in renminbi credit, it added.

Credit to non-banks in US

According to the Basel-based central bank for the world's central banks, the BIS locational banking statistics (LBS) show that banks' global cross-border claims fell by $377 billion on an FX (foreign exchange)- and break- adjusted basis in Q4 2023.

This pushed the outstanding stock of claims to $39 trillion, up 4% year-on-year (yoy), it said.

The Q4 drop was due to a $705 billion decline in the market value of derivatives and other instruments (-4% yoy), said BIS.

"The drop was also linked to seasonal factors whereby large banks headquartered in several jurisdictions tend to reduce their positions at year-end."

Looking across currencies, BIS said that cross-border dollar- and euro-denominated derivatives claims fell by a combined $590 billion in Q4 2023, as banks in AEs, most notably Germany, France and the Netherlands, reduced their claims on the United Kingdom, a major centre for derivatives clearing.

In contrast to overall claims, cross-border bank credit - which includes loans and holdings of debt securities but excludes derivatives - expanded by $319 billion in Q4 2023 (+6% yoy), as banks reported greater debt securities claims (+$284 billion or +13% yoy).

BIS said credit to borrowers in the United States, Canada and Spain rose the most, growing at double-digit rates on a year-on-year basis, pushing the growth rate of credit to all AEs to 7% yoy.

"Moreover, cross-border bank credit to EMDEs showed signs of recovery in Q4 (+$30 billion), with yoy growth rates turning slightly positive following three quarters of negative growth in 2023."

Much of the increase in global cross-border credit was driven by lending to non-bank borrowers, with credit to these borrowers growing by 8% yoy in Q4 2023, an annual rate not seen since early 2020, said BIS.

Within the non-bank sector, credit to the non-financial sector (NFS) rose by a notable $247 billion, it added.

On the other hand, BIS said credit to non-bank financial institutions fell by $16 billion, following a surge during the first three quarters of 2023 (+$600 billion).

It said that US dollar- and euro-denominated bank credit drove the growth of credit to NFS borrowers.

In Q4, credit denominated in these currencies increased by $130 billion and $87 billion, respectively, while yen-denominated credit edged down.

The biggest portion of new credit went to borrowers in the United States (+$144 billion), followed by those in Italy and France, said BIS.

"The bulk of the overall increase was booked by banks located in Japan, mainly as holdings of debt securities issued by the NFS in the United States."

US policy tightening

Cross-border bank credit denominated in US dollars recovered in 2023, after having declined during the previous year, said BIS.

It said the decline in 2022 coincided with a series of rate hikes by the Federal Reserve and a broad-based dollar appreciation.

"As the pace of policy tightening slowed in December 2022, the growth in dollar credit to AEs stabilised and returned to positive territory in the course of 2023."

At end-2023, outstanding dollar credit to AEs reached $12.1 trillion, nearly $625 billion above Q1 2022 levels.

On the other hand, BIS said that dollar credit to EMDEs remained subdued throughout 2023.

It said the recovery in cross-border dollar credit to AEs during 2023 reflected higher levels of credit extended to borrowers in the United States.

It said throughout 2022, outstanding cross-border loans barely changed, whereas non-resident banks' reported holdings of dollar-denominated bonds dropped.

It added that in 2023, the rise in cross-border dollar credit was driven by an expansion in both loans and holdings of debt securities - by end-2023, dollar credit to US borrowers had increased by $655 billion since the initial rate hike in Q1 2022.

This is reflected in the quarterly changes of banks' consolidated international claims on the United States, which reveal greater claims on the US official sector in 2023, BIS explained.

BIS said that cross-border bank credit to EMDEs rose by $30 billion in Q4 2023 after two consecutive quarterly declines, pushing the yoy growth rate back into positive territory.

Looking across regions, it said credit to borrowers in Latin America expanded the most (+$15 billion), followed by Africa and the Middle East.

In Latin America, cross-border credit to Brazil grew by $10 billion, mainly denominated in pound sterling (+$5 billion), while elsewhere in the region, banks channelled funds mainly to Mexico and Peru.

BIS said in Africa and the Middle East, banks reported greater credit to Saudi Arabia (+$10 billion) and Qatar (+$5 billion). In contrast, credit to borrowers in Israel declined (-$5 billion).

Bank credit to the Asia-Pacific region expanded modestly, by $4 billion. Credit denominated in renminbi surged, mainly to borrowers in China and Hong Kong SAR (+$29 billion combined).

At the same time, dollar-denominated credit to those two economies dropped by $12 billion, and that to Korea dropped by $11 billion, said BIS. *(SUNS 9999)*

US dollar credit to EMDEs saw up-tick in Q4 2023, say BIS

Reversing a decline in the third quarter of 2023, US dollar credit to emerging market and developing economies (EMDEs) rose by $12 billion in the fourth quarter, according to the Bank for International Settlements (BIS).

by Kanaga Raja

PENANG: US dollar credit to emerging market and developing economies (EMDEs) rose by $12 billion in Q4 2023, reversing a decline in Q3, the Bank for International Settlements (BIS) has said.

Reporting on its global liquidity indicators at end-December 2023, BIS said foreign currency credit in US dollars inched down in Q4 2023, while euro- and yen-denominated credit increased.

[According to BIS, its global liquidity indicators (GLIs) track credit to non-bank borrowers, covering both loans extended by banks and funding from global bond markets, the latter through the net issuance (gross issuance less redemptions) of international debt securities (IDS).

[BIS said the main focus is on foreign currency credit denominated in three major reserve currencies (US dollars, euros and Japanese yen) to non-residents, I .e. borrowers outside the respective currency areas.]

The $87 billion quarterly decline in US dollar-denominated credit to non-banks outside the United States left the outstanding stock just below $13 trillion, said BIS.

Nonetheless, it said that the yoy growth rate turned positive due to base effects.

Euro-denominated credit to non-banks outside the euro area increased by EUR 31 billion, which pushed the stock of credit just above EUR 4.1 trillion ($4.6 trillion), or 4% higher than a year earlier.

Following a pause in the previous quarter, yen-denominated credit outside Japan accelerated in Q4 due to a surge in bank loans, said BIS.

The outstanding stock, at 64 trillion yen ($451 billion), was up 16% from a year earlier, it noted.

Dollar-denominated foreign currency credit to non-banks in EMDEs showed signs of recovery in Q4 after several quarterly declines since 2022, BIS said, adding that the $12 billion increase in credit left the amount outstanding at $5.1 trillion.

Nevertheless, it said that yoy growth remained negative at -0.9%.

Looking across regions, BIS said dollar credit to borrowers in Asia-Pacific excluding China rose the most in Q4 (+$15 billion), followed by credit to those in Latin America (+$13 billion) and Africa and the Middle East (+$12 billion). In contrast, credit to China fell by $20 billion.

BIS said the differences in credit growth across the dollar, euro and yen reflect their respective funding costs and associated exchange rate developments.

"The negative co-movement between exchange rate indices and credit growth has been salient over the past few years," it noted.

BIS said monetary policy tightening by the Federal Reserve led to a stronger dollar throughout 2022, weighing on dollar-denominated bank lending and bond issuance.

"The European Central Bank's policy tightening triggered a similar pattern in euro credit growth from mid-2022 onwards."

Moreover, BIS said brisk growth in yen credit from early 2022 onwards went hand in hand with sustained yen depreciation as the Bank of Japan kept interest rates below zero.

The negative co-movement between exchange rates and credit growth was particularly evident for EMDEs, BIS pointed out.

The 0.9% yoy decline in dollar credit to EMDEs at end-Q4 2023 stood in contrast with the 0.9% global increase, it said, adding that the discrepancy was more striking for euro credit.

"In Q4, euro credit to all borrowers outside the euro area grew by 3.8% yoy, yet euro credit to EMDEs shrank by 0.8% yoy."

BIS said that yen credit to EMDEs continued to grow at 21% yoy, compared with a global pace of 16% yoy.

Nevertheless, as monetary policy tightening slowed in the United States and euro area in 2023, annual growth rates of credit began to converge towards those of the global aggregates, it added. *(SUNS 9999)*

Chronicle of a catastrophe foretold

In light of the recent warning by the International Monetary Fund of a decade ahead of "tepid growth" and "popular discontent", *Jomo Kwame Sundaram** has argued that little is being done multilaterally to avert the imminent catastrophe.

KUALA LUMPUR: The IMF warns of a decade ahead of "tepid growth" and "popular discontent", with the poorest economies worst off.

But as with inaction on Gaza, little is being done multilaterally to avert the imminent catastrophe.

Grim prognosis

Noting the world economy has lost $3.3 trillion since 2020, International Monetary Fund (IMF) Managing Director Kristalina Georgieva announced this grim warning before last month's Spring meetings of the Bretton Woods institutions.

Instead of prioritising economic recovery, finance ministers and central bank governors in Washington agreed to continue policies worsening the situation.

After all, curbing inflation helps preserve the value of financial assets.

Current policies suppressing demand are justified as necessary for financial stabilisation.

They do nothing to address the various "supply-side disruptions" mainly responsible for ongoing inflationary pressures.

These include the "new geopolitics", the COVID-19 pandemic, wars, illegal unilateral sanctions, and market manipulation.

Thus, ostensibly counter-inflationary measures have worsened pressures perpetuating stagnation.

The new Cold War of the last decade and other geo-political considerations increasingly shape economic and financial policies worldwide.

Powerful nations have weaponised their formulation, implementation and enforcement.

Years of economic stagnation have diminished productive and competitive capabilities.

Meanwhile, recent geopolitics has changed geoeconomic relations, hegemony and its discontents.

Laws, regulations and judicial processes are increasingly deployed for political – and economic – advantage.

Thus, Western governments have generated inflationary pressures with their economic and geopolitical policies, even if inadvertently.

Perceptions of strategic decline are mainly attributable to the ostensibly market-based policies pursued.

The European Central Bank has followed US Fed interest rate hikes from 2022.

Both still maintain high interest rates, ostensibly to keep inflation in check.

Unsurprisingly, most developing country monetary authorities have had to raise interest rates to reduce capital flight and bolster their exchange rates.

Such interest rate hikes by central banks have raised the costs of funds, squeezing both consumption and investment.

Raising interest rates has proved blunt and limited, while more appropriate measures have curbed inflation more effectively.

Instead of checking inflation due to supply disruptions, higher interest rates have squeezed both investment and consumption spending by both the private sector and government.

Such cuts have hurt demand, jobs and incomes worldwide.

Although interest rate hikes worldwide have been contractionary, other US macroeconomic policies since the 2008 global financial crisis have maintained full employment in the world's largest economy, with limited gains for most others.

Hands tied

Many developing country governments borrowed heavily in the late 1970s, mainly from Western commercial banks.

But after the US Fed sharply raised interest rates from 1979, severe sovereign debt distress paralysed many heavily indebted governments in Latin America and Africa for at least a decade.

Much more government borrowing, increasingly from bond markets in the decade before 2022, exposed many developing economies to debt stress.

This can be much worse than in the 1980s, as debt levels are higher, with more diverse creditors.

With borrowing exposure much higher and more market-based, with less from banks, debt resolution is much more difficult.

Many governments have also guaranteed state-owned enterprise borrowings, with some even doing so for well- connected private enterprises.

Meanwhile, policymakers in developing countries today are even more constrained by their circumstances.

Vulnerable to market vicissitudes and with fewer macroeconomic policy instruments available, they face pro-cyclical policy biases due to market pressures and supportive institutions.

Besides financial market pressures for fiscal austerity, multilateral financial institutions like the IMF impose such conditions on countries seeking emergency credit and other debt relief.

All this has led to deep government expenditure cuts, especially for public investments, crucial for recovery of the real economy.

Hence, governments commit not to spend despite the urgent need for such counter-cyclical expenditure.

Central bank independence typically implies greater sensitivity to market pressures and private financial interests rather than national and government policy priorities.

Instead of strengthening national capacities and capabilities, central bank independence and autonomous fiscal policy authorities have disarmed developing country governments in the face of greater external vulnerability.

This toxic mix may well keep vulnerable governments in protracted debt peonage, unable to free themselves from its yoke, let alone give them the room to create conditions for renewed growth.

Economic liberalisation and globalisation have irreversibly transformed developing economies, with lasting consequences.

Export opportunities have become

more limited, not least due to the weaponisation of economic policies.

Meanwhile, most developing countries have turned to private creditors despite higher interest rates and borrowing costs.

But even private market lending to the poorest nations has dried up since 2022 after the US Fed raised interest rates sharply.

With higher Fed interest rates, finance has abandoned developing countries for "safety" in US markets.

As debt service costs soared, distress risks have risen sharply.

Hence, many economies in the Global South are barely growing, especially after earlier collapses of commodity prices, which later worsened due to falling demand as supplies rose due to earlier investments. (IPS)

[* **Jomo Kwame Sundaram**, a former economics professor, was United Nations Assistant Secretary-General for Economic Development, and received the Wassily Leontief Prize for Advancing the Frontiers of Economic Thought in 2007.]

Thin and Shallow: Financial Instruments for Biodiversity Conservation and Their Outlook

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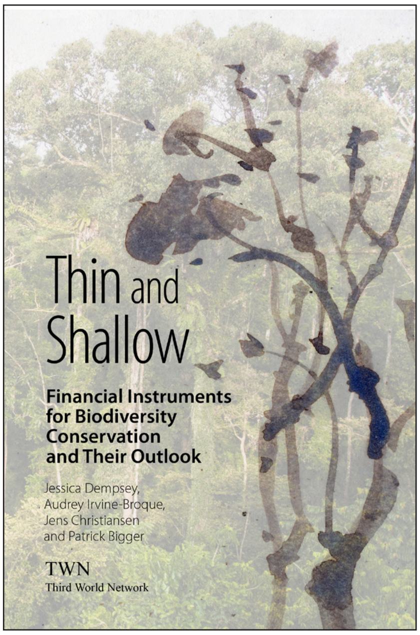

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This paper examines the track record of private financial mechanisms aimed at funding conservation of biological diversity. It finds that, due to lack of rigorous and consistent benchmarks and monitoring, these investments may not necessarily safeguard biodiversity and could even, in some cases, have adverse impacts. Further, despite decades of attempts to draw private capital to biodiversity protection, the quantum of finance remains limited, especially in the highly biodiverse countries of the Global South where it is most needed.

Written for a research project established by a group of central banks and financial supervisors, this paper cautions these authorities from deploying resources towards promoting such biodiversity-focused private financial instruments. Instead, the supervisory bodies are urged to step up policy coordination to address drivers of biodiversity loss in the financial system.

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