

# LUISS



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The Asian Infrastructure Investment Bank,  
Complementing or Challenging  
International Financial Institutions?

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## List of Abbreviations

AIIB	Asian Infrastructure Investment Bank
ADB	Asian Development Bank
AOA	Articles of Agreement
BRI	Belt and Road Initiative
BRICS	Brazil, Russia, India, China, South Africa
CDB	China Development Bank
CNM	Chief Negotiation Meeting
CPC	Communist Party of China
CCP	Chinese Communist Party
EEAS	European External Action Service
EIB	European Investment Bank
ERDB	European Bank for Reconstruction and Development
EM	Emerging Markets
EU	European Union
ESF	Environmental and Social Framework
EXIM	Export-Import Bank of China
FDI	Foreign Direct Investment
FTAAP	Free Trade Area of the Asia-Pacific
GATT	General Agreement On Trade and Tariffs
GDP	Gross Domestic Product
GEG	Global Economic Governance
IBRD	International Bank for Reconstruction and Development
IDF	International Development Finance
IFIs	International Financial Institutions
IMF	International Monetary Fund
MOFCOM	Ministry of Commerce
MDB	Multilateral Development Bank
MOU	Memorandum of Understanding
NDB	New Development Bank
OBOR	One Belt One Road

OECD Organization for Economic Cooperation and Development  
PPM Project-Affected People's Mechanism  
PPPs Public-Private Partnerships  
PRC People's Republic of China  
RCEP Regional Common Economic Partnership  
RMB Renminbi  
SCO Shanghai Cooperation Organization  
SDG Sustainable Development Goal  
SDR Special Drawing Rights  
SOE State-Owned Enterprise  
WB World Bank  
WTO World Trade Organization

## Abstract

The contribution of China to the world through major initiatives has been remarkable. China is pursuing domestic reforms and is trying to foster a new type of international relations based on win-win cooperation, mutual trust, and mutual respect. The concepts of China dream, community of shared destiny, shared future for mankind are meaningful. New initiatives have been launched in order to pursue connectivity between the old and the new world. From the Belt and Road Initiative to the Asian Infrastructure Investment Bank (here forward referred to as AIIB), the leader of the People's Republic of China, is bringing innovation in global governance. The underrepresentation of China and developing countries in the post-WWII international institutions and the dissatisfaction regarding failures in reforming the international financial system have led to the establishment of a new Multilateral Development Bank, the Asian Infrastructure Investment Bank.

Despite the good Chinese intentions to create from scratch a new constructive forum which could benefit developing countries, the new Bank was initially seen as more of a challenge. Since its negotiations, the AIIB has been able to attract not only developing countries but also and most importantly developed ones. Many EU member countries joined the Bank as founding members in order have an influence from the inside. Their contribution in expertise and technical assistance has demonstrated to be vital in fostering a new MDB that is following the rules. China has committed to a rule-based international system and is willing to provide global public goods. The AIIB can contribute to a positive impression of China to the Asian region and to the world.

The aim of this research is to investigate how the AIIB is pursuing multilateralism. This thesis argues and tries to prove that the AIIB is a successful ingredient that is complementing the international financial architecture.

**Keywords:** AIIB, Chinese foreign policy, Multilateral Development Banks, Neo-liberal institutionalism, GEG

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# Introduction

China's rise is shaping the global financial system. Its rise is posing some challenges for the "global financial architecture". China has worked together with established powers in order to reform some institutions such as the World Bank and the International Monetary Fund (IMF). At the same time, it has created institutions such as the AIIB which can compete and challenge the established global financial order.

China has been effective in reforming the international financial architecture, but at the same time, it has created new institutions in order to fill the deficits of the existing ones. Right now, cooperation is based and pursued upon principles such as additionality, complementarity and comparative advantage. In this context it is worth to examine the nascent AIIB in the realm of development finance.

The AIIB, 亚洲基础设施投资银行 or 亚投行 (in standard Chinese Yàzhōujīchǔshèshītóuzīyínháng or Yàtóuháng) is an example of this new policy. The first China-led Multilateral Development Bank, the Asian Infrastructure Investment Bank (AIIB), was first announced in October 2013 in Indonesia when Xi Jinping highlighted the willingness to implement new policies related to the Belt and Road Initiative (BRI). The proposal came after President Xi Jinping announced the Silk Road Economic Belt during a visit in Kazakhstan in September 2013. The two initiatives, the BRI, and the AIIB, respectively, are deeply linked together since the AIIB will be a source of funding for the BRI.

The AIIB will play a significant role in shaping China's regional and international influence in more than one way. This bank is pivotal for China's leadership and as a diplomatic initiative. Moreover, it will help the relations between Asia and Europe. But amongst all the countries, the United States will likely be the most affected, especially on the diplomatic sphere<sup>1</sup>. Many scholars argued the nature of the China-led initiative, and although proponents of power transition theory and offensive realism see the AIIB as an

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<sup>1</sup> Lipsy (2015)

initiative that will challenge and undermine the existing financial order, neo-liberal institutionalists have a more positive view on this issue.

### Research question and hypothesis

My hypothesis is that China is not challenging but rather modifying the existing multilateral international institutions. My research question is whether the AIIB is challenging the existing multilateral financial institutions or not. In order to deliver a comprehensive and exhaustive answer to the research question, this thesis is structured in the following way.

### Research Structure

Firstly, I will analyze the literature I have utilized for the findings. Secondly, I will outline the theoretical perspective that supports my argument, and then I will divide the main body into four sections. The first chapter will take into consideration neo-realism and neo-liberal institutionalism with a particular focus on the latter being the theory on which the AIIB is institutionalized. Moreover, the concept of contested multilateralism will be outlined and used to prove that the AIIB is not following this theory, but instead, as it currently stands it is pursuing, multilateralism. The second chapter will have a focus on the reasons that pushed Beijing to establish the AIIB, the correlation between the OBOR and the AIIB initiatives <sup>2</sup>. In addition, it will take into consideration Chinese internal and foreign policy goals, presenting the One Belt One Road initiative (OBOR or Belt & Road or B&R) and the reasons behind the launch of the AIIB. Moreover, the AIIB functioning and modus operandi will be explained, through the help of figures, and a detailed analysis of the Bank's Articles of Agreement. The third chapter will analyze the success this Bank had, explaining why the AIIB is not challenging but rather complementing the existing financial order by emphasizing the cooperation through co-financed projects with existing MDBs and an analysis of its competitors such as the Asian Development Bank and the New Development Bank. In addition, it will also be investigated with the example of two case studies, why regional and non-regional countries joined the AIIB, these being the main factors of success and a confirmation of the multilateral feature of the Bank. I chose India and the UK on purpose, because these

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<sup>2</sup> Gabusi (2017)

two countries though having different backgrounds, they have a common denominator, both were founding members of the AIIB. The fourth section will take into consideration the European Union and China's views on global economic governance. Moreover, the Chapter introduces how, in the framework of the AIIB, there can be an enhanced cooperation between the EU and China for the purpose of reforming global economic governance.

The aim of this work is to analyze the factors that identify the new Bank as a complementary ingredient to the global financial governance; therefore, the hypothesis is analyzed through the neo-liberal institutionalists' theories.

## Literature Review

In order to accurately answer the research question, this section of the thesis will cover the findings of my research and point out the main ideas the scholars have highlighted in their works. There has been an ongoing heated debate regarding the multilateralism of the bank, and a large body of literature has investigated the AIIB since it was established<sup>3</sup>. The first strand of research concentrates on China's motivation to launch the AIIB, and according to some scholars, the main reason was the "thirst for infrastructure funding" globally but with a specific focus on Asia's demand for funding. And because of the lackings of the existing development financing architecture that was not able to meet the demand in the Asia region, the AIIB was able to fill the gap<sup>4</sup>. In addition, also other scholars noted the frustration of China with the lack of global economic governance reform, and the AIIB was created in order to promote reforms<sup>5</sup>. Some scholars view the China-led AIIB as a gradual modification of the Asian financial order and a contribution to global governance. As a matter of fact, according to Cai<sup>6</sup>, the two diplomatic initiatives, the One Belt One Road (OBOR) and the Asian Infrastructure Investment bank (AIIB), are strictly related together and will promote regional and global economic cooperation.

Moreover, these two initiatives will not only help to promote Chinese influence, but they will also have a significant impact on the economic architecture in more than one area, regional and non-regional, respectively. Park<sup>7</sup> states that the China-led AIIB can represent a gradual modification of the Asian financial order. Another confirmation of this view is that this initiative can be seen as a rebalancing measure of global economic governance and that rather than seeking to replace the existing banking institutions, the AIIB will learn from them and promote the development of the world economy by providing "global public goods". Similarly, according to some scholars such as Gransow<sup>8</sup> and Hanlon<sup>9</sup> concerning the process of institution-building, China followed the rules to

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<sup>3</sup> Callaghan and Hubbard (2016)

<sup>4</sup> Takatoshi (2015)

<sup>5</sup> Zheng and Liu (2018)

<sup>6</sup> Cai (2018)

<sup>7</sup> Park (2017)

<sup>8</sup> Gransow (2018)

<sup>9</sup> Hanlon (2017)

alleviate the rising concerns of the Western world and give legitimacy to the AIIB. Besides, whether the AIIB will bring a change in the regime or follow the rules, according to Harpaz<sup>10</sup> since Beijing has benefitted from the status quo system it will not undermine it; however, it's approach of "no political strings attached " means that China is not playing by the same rules as traditional donors.

## **Research Methodology**

Different materials have been analyzed in order to conduct this research. In order to deliver an answer to the research question many academic papers, official documents and statistical data have been reviewed.

The Articles of Agreement of the AIIB were consulted in detail in order to develop an exhaustive analysis of the Bank's purpose, shares, and voting distribution not only in its governance but also in its structure.

In addition, other similar documents have been used to evaluate the current joint projects the Bank is developing with other MDBs. These documents have been useful, as a primary source, to gather the most accurate data possible. Information is sourced and gathered through reports, interviews, academic production and specialized articles. Moreover, being an institution established in 2015 while conducting the research many new official documents and reports were released leading to further developments in the status of the AIIB and how it operates.

Moreover, reports and scholar's papers were utilized to learn both the financial implication and the political one. Official documents, such as the Memorandum of Understanding, also helped deliver a qualitative research of multilateral development banks' main functions. Interviews with specialists of the Bank, Professors of China Foreign Affairs University and further discussions coming from international media and scholars' opinions were valuable sources during the research to strengthen the thesis' conclusions. An overview of both Chinese and European perspectives is the main pillar of this work.

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<sup>10</sup> Harpaz (2016)

# Chapter 1 Theoretical Framework

## 1.1 Neo-Realism

Neo-realism develops from the theory of realism and addresses new issues which have come up in the international system. In general, neo-realists focus on issues of military security and war. In order to explain this theory, we can refer to Kenneth Waltz's Theory of International Politics<sup>11</sup>. The theory of Waltz<sup>12</sup> highlights the importance of the structure of the international system and the role of the state in it. According to the structure of the international system, foreign policy will be shaped. Waltz assumes that the ordering principle of the international system is anarchy and capabilities are distributed across states. States are differentiated in the international order according to their power. Since the system is anarchic, the issue of security arises, sometimes resulting in the security dilemma. The political scientist does not believe in managing the challenges of globalization by building effective international institutions. As a matter of fact, the effectiveness of the latter depends mainly on major powers' support. Generally, neo-realists agree that states and actors interact in an anarchic environment without a central authority that enforces rules and norms to protect the interests of the community. Actors will behave according to the structure of the system. Moreover, zero-sum games are the outcome.

Most importantly, states are rational actors, self-interest oriented and favor self-help over a cooperative behavior. Their survival is what matters the most, and the situation of distrust and fear leads to the security dilemma. Conflict is unavoidable in some cases. Neo-realism regarding security studies is further divided into defensive realism and offensive realism. While on the one hand, defensive realists believe in cooperation as a tool that can be used to avoid conflicts, offensive realists highlight the importance of relative power.

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<sup>11</sup> Waltz (1979)

<sup>12</sup> Ibidem

## **1.2 Neo-Liberal Institutionalism**

Usually, in the academic world, neo-liberal refers to neo-liberal institutionalism. This theory shares many core assumptions of neo-realism. However, in contrast to neo-realists, the adherents of the institutional theory focus more on issues of cooperation, international political economy, and institutions. Instead of focusing excessively on conflict, neo-liberal institutionalists have a different view of cooperation. As a matter of fact, institutions are seen as mediators and as a mean to achieve cooperation and participation in an anarchic world. Scholars such as Graham Allison (2000) and Robert Keohane (2002) support the idea of creating regional and global regimes that promote cooperation and coordination among states in order to provide a collective response to new security threats<sup>13</sup>. Multilateralism is advocated over unilateralism.

To sum up, according to neo-liberal institutionalists, the main assumptions are that states are key actors in international relations, but also non-state actors are taken into consideration. States seek to maximize absolute gains over relative ones through cooperation, and they are willing to cooperate because they have mutual interests. However, since actors try to achieve absolute gains, “cheating” or non-compliance by other states may occur.

## **1.3 Contested Multilateralism**

North defines institutions as “the rules of the game in a society or, more formally, the human constraints that shape human interaction”<sup>14</sup>. What makes institutions successful are different factors. These factors are the ability to reduce costs for participants compared to the status quo, the existence of authorities overseeing the enforcement of agreements, reputation, and the time horizon of its members.

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<sup>13</sup> Baylis et al. (2014)

<sup>14</sup> North (1990)



Moreover, institutions are perceived as an answer to “time inconsistency,” a tendency to not honor commitments taken in the past as actors often value a short-term goal more than a long-term one. Furthermore, institutions are tools to allocate power and veto powers.

As it currently stands the AIIB does not pose a situation of contested multilateralism. The concept of contested multilateralism describes conditions under which multilateral institutions are challenged by counter policies pursued by actors, such as states, multilateral organizations, and non-state actors that are dissatisfied with status quo institutions. Contested multilateralism can happen when there is a shift in a regime a competitive regime is created.

Keohane defines multilateralism as “the practice of coordinating national policies in groups of three or more states, through ad hoc arrangements or through institutions”<sup>15</sup>. However, multilateral institutions can face challenges when other multilateral institutions pursue unilateralism or bilateralism. When the parties propose responses that are not suitable, and they create formal or informal institutions that are not in line with the status quo, a situation of contested multilateralism is likely to occur. Moreover, since according to Keohane multilateral institutions are “multilateral arrangements with a persistent set of rules”<sup>16</sup>, both definitions emphasize the state as an actor and the rule-based institutional arrangement of multilateralism as elements in multilateralism that are manifested by the mechanisms of the AIIB. Therefore, the institution of the AIIB as it currently stands does not pose a scenario of “contested multilateralism” that Morse and Keohane theorized. According to Morse and Keohane<sup>17</sup>, three criteria define a situation as involving contested multilateralism. Firstly, “a multilateral institution is conceived within a defined issue area and with a mission and a set of established regulations and institutionalized practices<sup>18</sup>”. Secondly, a coalition of actors dissatisfied with the status quo institution tries to shift the focus of it by adopting new rules and practices embedded in a new challenging institution. Thirdly, contested multilateralism is fulfilled if the practices and regulations of an institution are challenging because they conflict or extremely modify the practices and rules of a status quo institution. While the AIIB fulfills the first criteria, it does not satisfy the second. And, as it will be discussed, the

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<sup>15</sup> Keohane (1990)

<sup>16</sup> Keohane (1990: 732)

<sup>17</sup> Morse and Keohane (2014)

<sup>18</sup> Ibidem

AIIB follows traditional practices of the status quo institutions and the activities of the AIIB do not shift focus away from institutions like the World Bank. Instead, they complement the development efforts in Asia.

However, a significant shift can be detected in the restructuring of global economic power. From the Chinese perspective, the reform of the global governance system is not about dismantling the existing system and creating a new one to replace it. Instead, it aims to improve the global governance system in a more innovative way following the expertise of the existing MDBs. Now I will analyze in detail the complementary approach of the AIIB being institutionalized on multilateralism.

#### **1.4 Complementing International Financial Institutions**

In order to accurately answer the research question, an IR explanatory theory is needed. A debate over Chinese revisionism and status quo based on IR theories is ongoing. Regarding the AIIB China-led initiative, this thesis argues that this new multilateral development Bank can be seen as a modification of the existing Asian financial order. According to Park<sup>19</sup>, four strategic approaches to AIIB can be found. The mainstream approach sees the division into two groups. While on the one hand, this new institution generated a lot of concern in the United States and mainly other Western countries, on the other hand, it represents a positive outcome to Asian developing countries. In the first group of countries, American and Japanese policymakers perceive the AIIB as a threat to the status quo and as a challenge to the US-led international economic order, in particular to the established Western-dominated financial institutions such as the International Monetary Fund (IMF), the World Bank and the Asian Development Bank.

According to them, China is trying to create an alternative architecture to the established one. This view can be linked to the proponents of transition theory and offensive realism, such as Robert Gilpin, and John Mearsheimer. Some proponents say that states when rising are mainly revisionist powers. Also, Gilpin<sup>20</sup> declares that states are self-interested power maximizers, and since there is no global government, the rising state will likely undermine the status quo. According to Mearsheimer<sup>21</sup>, all great powers

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<sup>19</sup> Park (2017)

<sup>20</sup> Gilpin (1984)

<sup>21</sup> Mearsheimer (2001)

are revisionist because they pursue their survival and security, and since the international system is anarchic, this leads them to achieve relative gains over the absolute ones.

On the other hand, developing countries have more optimistic views. They claim that the new MDB would play a complementary role to the existing institutions rather than undermining them.

Moreover, these views are based on other theoretical perspectives, the ones of neo-liberal institutionalists, such as Robert Keohane and John Ikenberry. In contrast to what the proponents of transition theory and offensive realism claim, Ikenberry<sup>22</sup> states that rising powers are not revisionist powers because institutions are perceived as the means to pursue mutual gains. The debate over China's role as a status quo power or a revisionist one has been central, and the following paragraph will analyze Chinese multilateralism in the AIIB.

The Asian Infrastructure Investment Bank is institutionalized on multilateralism. However, Chinese multilateralism is different from American multilateralism, which is embedded in the institutions created in 1944 with the Bretton Woods agreement. The new Bank aims to position itself in a complementary role in the existing multilateral development financing<sup>23</sup>. The AIIB is, therefore, the result between Western and Chinese principles of cooperation and development. Even the Bank's President-designate Jin Liqun stressed the principles mentioned above in several occasions. During the whole process of drafting of the Articles of Agreement shareholders have been working collegially to formulate the underlying principles of the bank such as transparency, openness, accountability, and independence. Besides, the guideline of the operations will have a strong policy and governance framework. Moreover, the AIIB will bring innovation in infrastructure financing suitable for Asia's infrastructure needs. The Bank will also join the MDBs family contributing to the social development in Asia with investment based on sustainable infrastructure<sup>24</sup>.

The features of multilateralism in the agenda of the AIIB can be strongly detected not only in its constitutional charter but also in the standards. Recalling the definition of multilateralism by political scientist Ruggie, multilateralism is an "institutional form that

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<sup>22</sup> Ikenberry (2008a)

<sup>23</sup> Gu (2017)

<sup>24</sup> Ong (2017)

coordinates relations among three or more states on the basis of ‘generalized’ principles of conduct—that is, principles which specify appropriate behavior for a class of actions, without regard to the particularistic interests of the parties or the strategic exigencies that may exist in any specific occurrence”<sup>25</sup>. Multilateralism has two potential results, which are indivisibility and expectation of diffuse reciprocity<sup>26</sup>. The AIIB’s slogan and modus operandi are “lean, clean, and green,” and accordingly these words are specifically the three defining keywords of the Bank; lean, with a highly skilled staff; clean, the ethical modus operandi with high standards of anti-corruption; and green, the pillar of this institution which takes cares of the environment and respects it.

Moreover, multilateralism fosters predictability, transparency, and sustainability, generating “diffuse reciprocity,” which is expected to benefit the AIIB membership. In the law of the AIIB, multilateralism is fulfilled in the decision-making process. Consensus-seeking has always been present from the beginning of the establishment of the Bank; in particular, from the signing of the Memorandum of Understanding in 2014 to the official establishment of the AIIB on 25 December 2015. All matters from the initial phase to the formal establishment of the new multilateral institution have been decided by consensus. The consensus approach is also present among the three existing institutions of global economic governance – the IMF, the World Bank, and the WTO. Although the formal provisions of these institutions provide majoritarianism in the treaties, whenever possible consensus is sought in the decision-making. The IMF and the World Bank have a label of “one dollar-one vote” and the WTO “one-Member-one vote”<sup>27</sup>.

The Bank has a nonresident director system which allows prioritizing developing countries’ needs and these countries to have their voice heard. However, when consensus is not possible for decision-making, voting is the best option. Especially in the decision-making of the AIIB when consensus fails, a 75% affirmative vote is applied.

Furthermore, the AIIB provides a three-class voting system, a simple majority, a “Super Majority” for essential issues<sup>28</sup> and a “Special Majority” for special topics such as the establishment of a Bank subsidiary<sup>29</sup>. The mission of the AIIB is to reflect the views, voices, and values of all its shareholders as underlined several times by the

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<sup>25</sup> Ruggie (1992)

<sup>26</sup> Ibidem

<sup>27</sup> White (2005)

<sup>28</sup> AIIB AOA article 28.2

<sup>29</sup> AIIB AOA Article 16.8

President of the Bank, Jin Liqun. However, China has a de facto veto power on issues such as the decisions on the size of the Board of Directors, any amendment of the AOA and the election of the President, all of which require a Super Majority vote. The number of veto players in a system has an impact on its capacity of making decisions and on its stability. In opposition to the US' power in the IMF AOA, there is no similar situation in the AIIB symbolizing China' s transparency in not seeking veto power in the Bank.

Another key element that explains the result of the merging between Chinese and Western principles of cooperation can be detected in the decision of many OECD countries to join the AIIB. The OECD is an intergovernmental forum that allows for collaboration among members of governments on economic, social, and environmental topics. From the beginning, they contributed and cooperated providing OECD principles regarding rules and procedures that were discussed during AIIB's preliminary negotiations. The cooperation between developing and developed countries and the participation of all the shareholders to contribute to the creation of something new based on principles and a good governance structure was the major success of the Bank.

## **Chapter 2 Why The World Needs The AIIB?**

### **2.1 The Bretton Woods System**

The system of Bretton Woods was a first attempt to establish an international monetary order with fixed exchange rates. This system was designed in order to develop a new exchange rate and international payments policy to avoid the problems that arose during the Great Depression. It was conceived as a compromise between John Maynard Keynes, at the time adviser to the British Treasury, and Harry Dexter White, the chief international economist at the Treasury Department. The system designed at the conference at Bretton Woods in July 1944 was a first attempt to forge an international monetary order with fixed exchange rates based on an international treaty. Delegates from forty-four countries gathered in Bretton Woods, New Hampshire, agreeing to establish the International Monetary Fund which after became the World Bank Group. After the US Congress passed the Bretton Woods Agreement, President Harry Truman signed it on 31 July 1945. 28 countries signed the Articles of Agreement on 27 December 1945, and the Bank began its operations on 25 June 1946. The Soviet Union did not join the IMF and the World Bank. Policies for international economic governance were adopted through the founding of several international organizations. The GATT and after WTO promoted coordinated trade liberalization among all adherent states, the IMF was created in order to guarantee a system of fixed exchange rates and loans to help those countries which were hit by adverse economic shocks. During that time, the US Dollar was convertible to gold, and all the other currencies were pegged to the US Dollar. The World Bank had the main aim of financing the reconstruction in countries damaged by the war.

The Bretton Woods agreement established a system in which all the currencies were pegged to the US Dollar, and since the dollar was convertible to gold, the US de facto managed the monetary policies of all the members of the Bretton Woods System. The International Monetary Fund was designed to monitor exchange rates, lend reserve currencies to countries with balance-of-payments deficits, and encourage members of eliminating trade restrictions. Furthermore, another institution was established, the International Bank for Reconstruction and Development, now the World Bank Group

which was responsible for providing financial assistance for the post World War II reconstruction and help the economies of less developed countries. The system of currency convertibility lasted until 1971. It was an unprecedented effort coming from countries in order to establish a new financial order that could benefit countries involved in the second world war and overcome the crisis. The postwar architecture advantaged the major Allied powers of World War II, and China has always been underrepresented not only in the voting rights of the IMF but also the presence of Chinese nationals among major organizations was lacking<sup>30</sup>.

Why MDBs seek to reform? The system of the Washington Consensus pushed for the diffusion of neoliberal ideas and policies which became spread globally only in the 90s. Those multilateral rules were formulated inside the EU, the OECD, and the WTO. However, the aim of those rules was not to revolutionize the nature of the policies of supranational economic integration, but instead to standardize them so that no country was excluded from their potential benefits. Beyond the Washington Consensus, we find the European and Beijing Consensus. The European Consensus focuses on a package of measures aimed at primarily favoring development policies in EU's partner countries, and they are centered on three main sectors. These sectors include poverty reduction, development based on European democratic values, and accountability of developing countries for their future. The Beijing Consensus has been advanced as a sovereigntist alternative to the Western recipe that conceives in a non-negotiable way free market with democracy and human rights. On the contrary, for the Beijing Consensus, economic development has to be kept separated from the political sphere. The focus is a commitment to innovation and constant development, GDP as the only parameter to take into consideration for measuring progress and the pursuit of self-determination in terms of public policies.

The diffusion of this new setting, especially in the framework of the policies of the AIIB is the result of the decline of the Western powers. The doctrine of Beijing is emphasizing the development of local enterprises with the aim of self-development, providing aid without political strings attached and pursuing common development based on equality and mutual benefits and finally to keep pace with reforms and innovation. The One Belt One Road Initiative supports the spread of the Beijing Consensus. Opposite to the current success of the Beijing Consensus, the reasons for the weakening of the

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<sup>30</sup> Lipsey (2015)

Washington Consensus can be grouped in two essential dynamics. Firstly, the frequency of crises the South has experienced shows the weakness of the project of financial liberalization, and secondly the rising of social inequality due to the effects of the neoliberal reforms in numerous contexts. Both the World Bank and the International Monetary Fund were established during the negotiations at Bretton Woods in New Hampshire in 1944.

The World Bank was created following the American plan, and contrary to the United Nations General Assembly, both the members of the IMF and the WB did not have equal voting power. The WB had 38 members in 1946, now it is known as the World Bank Group and has 188 members in its International Bank for Reconstruction and Development (IBRD) and 172 members in its International Development Association (IDA). Many critics have been made to the Bank, in particular for its structural adjustment loans that worsened poverty in indebted developing countries. Japan successfully created the ADB, which is a hybrid of the World Bank and the Japanese institutions. The Japanese while building the ADB followed the World Bank experience. The China-led AIIB will be faster and flexible than the existing financial institutions, which will likely be pushed to reform. The AIIB is a functional equivalent of the World Bank and the ADB; however, it is pushing for a no more western-led international structure. The World Bank has implemented reforms regarding the internal governance i.e., “voice reforms.” Despite the reform in the share of votes held by developing countries, the weight of developing countries’ voting shares has not increased substantially. Compared to the United States, Japan, and European Union members, the influence of rising powers is not relevant. Taking as an example the case of China, since the 1970s its influence has increased within IOs. The international development finance architecture is no more centralized, but it has decentralized through structural shifts, and a plethora of multilateral development banks has come up. Through the nascent AIIB, the Asian institutional landscape is on the way of transformation.

Asia needs more infrastructure and international financing and the rapid growth and growing interdependence explain the demand for infrastructure. As a consequence, the demand for reform of international financial institutions is needed. President Xi Jinping emphasized the desire of stabilizing the world economy through multilateral cooperation. Moreover, while deepening economic ties with neighboring countries through the OBOR initiative, Beijing intensified the engagement with the Bretton Woods institutions. For many years, China has denounced the failure of the international



financial institutions that have not recognized China's weight in the global economy. According to Weiss<sup>31</sup>, many Members of the US Congress have perceived the AIIB as a China's response to the delay of the IMF approval of governance reforms. As a matter of fact, in 2010, the US Congress did not approve the package of reforms until 2015. Christine Lagarde, Managing Director of the IMF, was concerned with the delicate moment and announced that if the US Congress did not approve the reform, China would create a new Asian IMF.

## 2.2 China's overcapacity and the AIIB

China's problem of overcapacity relates to the recently announced initiatives such as the OBOR. In economic terms, overcapacity is a situation in which the supply exceeds the demand. China's overcapacity is linked to State Owned Enterprises, a functioning model in which all the Chinese GDP was a result and product of the export capacities. The GDP was not the product of Chinese consumption, but what China was selling to the world. In the 1970s the system changed, the production system adapted according to new preferences but still a lot of inefficiencies were characterizing this system, for example, highly energy-intensive industrial processes. A lot of negative externalities and inefficiencies defined this production system obsolete. Chinese authorities have taken some actions in order to reduce the country's overcapacity issue, especially after the financial crisis of 2007-08. China is addressing overcapacity through domestic reforms as well as through broader restructuring of the economic model. In October 2013 and in advance of the Third Plenum of the 18th National Congress of the Communist Party of China Central Committee, the State Council began to address the issue and introduced price reforms for water and electricity. The Decision of the Third Plenum stated that "a long-term mechanism will be established and improved for preventing and dissipating excess production capacity"<sup>32</sup>. Moreover, according to the Decision<sup>33</sup>, it was stated that the market had to be allowed to play a decisive role in the economy, and overcapacity was recognized as a priority for the central government. The 2015 Central Economic Work Conference recognized and identified the problem that China was facing as one of

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<sup>31</sup> Weiss (2017)

<sup>32</sup> China.org (2014)

<sup>33</sup> Ibidem

the top five priorities for 2016<sup>34</sup>. However, China's overcapacity was a problem already before 2008, and since the country was not fully integrated into the global economy, its overcapacity went broadly unnoticed. In late 2008 exports collapsed as a consequence of the entrenchment of the economies of the EU and the US and a growing gap between a stagnant global demand and an increasing domestic production capacity highlighted the problem of overcapacity. China's response was a massive fiscal stimulus package with an extensive lending program. In the short term, these policies boosted the economy, but in the medium term, they worsened the economic situation. According to the European Chamber of Commerce <sup>35</sup>, eight key industries experienced overcapacity: crude steel, cement, electrolytic aluminum, chemicals, refining, flat glass, shipbuilding and paper, and paperboard. The Chinese economy was mostly affected; however, the global economy also suffered, and tensions started to increase between China and trading partners. The country is making a transition from a mainly export-led economy to a more balanced strategy. Producers have an oversupply capacity and domestic markets which are limited. The new initiatives, the establishment of the Asian Infrastructure Investment Bank and the One Belt, One Road will help solve the problem of overcapacity. As a matter of fact, China can export its excess production to neighboring countries. This thought was advocated by a former Chinese Vice Foreign Minister, He Yafei. He published an article in the South China Morning Post outlining a plan to export excess capacity which should go hand in hand with a "going out" strategy to help the internationalization of Chinese companies. He acknowledged the potential effects of overcapacity and stated that "If left unchecked, it could lead to bad loans piling up for banks, harming the ecosystem" <sup>36</sup>and could even have a negative impact on society in the country's transition to a new growth model.

In the twenty-first century, the Chinese government started the "going out" policy to encourage Chinese companies to invest abroad through foreign direct investment. According to Cai <sup>37</sup>, the OBOR and AIIB initiatives will help China to find a new stimulus of growth and achieve strategic objectives i.e., economic and diplomatic. Moreover, by expanding external markets, Beijing can address and overcome the problem of the nation's industrial overcapacity, which has affected many industries. Beijing does not just

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<sup>34</sup> China Daily (2015b)

<sup>35</sup> European Chamber of Commerce (2016)

<sup>36</sup> He (2014)

<sup>37</sup> Cai (2018)

have to find a solution to China's overcapacity but more in particular to improve internal consumption. The Chinese government has reduced taxes in order to promote consumption, reduce dependency on imports and exports. They are trying to diversify the economy and the citizens' consumption. Furthermore, the income in China has experienced an increase, and China is a country that made a lot of progress on poverty reduction. However, being a command economy, it has undergone many weaknesses. Notwithstanding the current significant role of the state in the economy, in the future it is expected to become more marginal.

Because of all the overcapacity issue, another motivation for starting the AIIB is that China has a lot of capital to go around and investing in its own infrastructure and businesses is only so efficient. It's smart business sense to diversify and seek investment in other sectors to increase returns. China is able to use its capital gained from State-Owned Enterprises for investment in the MDBs. By creating their own MDB, they get more input into where that money goes, and therefore, more influence in the development of countries, perhaps prioritizing those in the BRI.

The difference between a State-Owned Company and a private one is that a SOE always has credit while the private one doesn't. So, the difficulty that now China is experiencing is linked to the inefficiency of the SOE in the market. All the fiscal stimulus measures addressed to the private sector have the goal to affirm the private sector.

In order to understand better the concept of Chinese state capitalism, it has to be underlined that it is state capitalism not because it doesn't want the private sector, but it is state capitalism because the state is present and plays a significant role in the market mechanisms. So, a difference lies also in the stock exchange market, if the stock market is not efficient in Europe new policies are tried to be implemented, on the reverse, in China if the stock market is not working efficiently state banks are backed by the state, and they can buy shares. Moreover, in all the productive structures in China, there is a section dedicated to the Communist Party, the state can also be a minority shareholder. But also, if the state is not present in the corporate structure of a company, it means that it is not state capitalism. Once again, the state capitalism is defined when the functioning mechanism of an economy are and must be authorized or liberalized by the state. Since in China everything must be authorized by the state it is not a market economy because the market does not have a normal operating mode. Open markets have other modalities. Today whoever invests in the Chinese market is aware of the fact that the market would never make choices, but there will always be another player. The risk level is diverse.

Also, now, with the litigation between the United States and China, the Chinese government took some counter-measures such as a control on exports. If there was the free functioning of the market, many more factors of production were involved and could limit the outcome.

### **2.3 A New Foreign Policy**

New major initiatives within regional and global governance have been pushed forward to strengthen the international role of China. New ideas and ideological narratives regarding Chinese foreign policy are fundamental in order to understand the new global vision of China's international politics. China is rising and is seeking higher power. Chinese domestic politics is intermingled with its foreign policy. Complementary to Track I diplomacy, more think tanks were established, not only sponsored by the government but also supported by private funding. If they have enough funding and good *guanxi* connections, they are usually affiliated to a university or an official think tank because that will give them convenience in connecting with the government. To be influential, they need to have some influence in the government so they usually would be affiliated with a university.

Regarding China's neighborhood diplomacy, Le Keqiang, current Premier of the state council of the People's Republic of China, promoted multiple partnership and organizations such as ASEAN plus China, ASEAN plus three and also the East Asia Summit.

Back in the 1976, the Tiananmen incident isolated China from the West and Deng Xiaoping said in that precise moment that China should keep a low profile, firstly focus on stabilizing the situation and secondly, not to take the lead internationally, but focus on economic development. In 1992 he went to the Pudong and Shanghai area which after 1992 speeded up its development and experienced an outgrow with Hong Kong. Then at that time, the leader adopted a practical and pragmatic attitude, he recognized the limits to China's capabilities, and later after the 2008 international financial crisis, China became the second world economy. In 2009 the G2 idea came up, a China-America partnership, but China was not prepared for this and in Copenhagen in 2009 refused to accept. It was not in the mindset; it was not the time to show the world China's more

significant responsibilities. But then in few years when China continued to develop, and the economic performance in comparison with other countries was excellent, the leader pushed for a more proactive China in taking up international obligations and try to provide public goods but at the same time continue to keep a low profile. In a few years when Xi came to power, he addressed natural rejuvenation, meaning that China was getting closer to the center of the international stage and pushed for this kind of discourse. There was a significant change of attitudes, on the one hand, it is true that at that time they had to commit more to the international society for example with the Paris agreement, but at the same time, China had so many challenges at home. Also, from 2010 to 2016, the situation in China's neighbors in Southeast Asia worsened because of South China Sea issues. It was also a time when the tension was built up from both sides. From the side of neighboring countries, they were sensitive to China's growth, and when the United States came back, the US encouraged neighboring countries to take a more confrontational approach against China, for example, Japan nationalized the Senkaku islands, and also the Philippines experienced a stand-off. The Philippines, Vietnam, Japan, and Taiwan played these cards mainly. On the side of China, the leadership changed saying that in the past they engaged primarily on neighboring countries with economic activities and now it was time for China to speed up the modernization of the country and develop a deep blue navy. So, for China's side, this was also more aggressive, however, the countries involved in the South China Sea dispute were claiming the lands. Also being China an infrastructure power, this was intimidating the neighbors. Myanmar in 2011 experienced a democratic transition and immediately distanced from China, pushing for Track I official meetings, and Track 2 meetings.

After the situation stabilized China and Myanmar agreed on building the China-Myanmar corridor connecting the north of Myanmar to the south. It is a wide shape corridor, which runs from the developed area to the Indian ocean. Moreover, the deep sea port of Myanmar will lead to China's access to the Indian port. This project is part of the OBOR initiative. Countries in these regions still have a high demand for investment and growth, because, without growth, governments don't have legitimacy; this is the immediate concern, China's neighboring countries have an urgent need of development. Manila used to be a very booming city and the growth rate has been quite high, one of the fastest growing economies in South East Asia, even in the world. Since they needed investments, they got closer to China. For countries such as China, and South East Asian countries, because they had a turbulent past, being invaded and colonized, the people and

the states very care sensitive of foreign intervention, whichever government could give them a better life is a good government. Legitimacy relies very much on economic growth. Regarding human rights for them, the right to development is the most important one.

According to the Foreign Policy Analysis theory, domestic situations spill over to foreign policy, conditioning and constraining it. It was only in February 2017 the momentum in which the Chinese President, Xi Jinping, underlined the new country's approach towards international relations namely the "two guides" policy (*两个引导 lianggeyindao*) regarding the new world order and global security. Many initiatives have been established since the Leader took office at the end of 2012. Apart from the AIIB, the new Silk Road Fund was announced, an investment fund established in 2014 with the support of the State Administration of Foreign Exchange (SAFE), China Investment Corporation, Export-Import Bank of China and China Development Bank; moreover, also think tanks such as the Silk Road and the Silk Road Think Tanks Alliance (SiLKS) were found. Furthermore, all these new initiatives are the result of a new Chinese approach to the world. China is also pursuing new neighboring policies such as the RCEP, Regional Common Economic Partnership. The modern neighboring diplomacy within regional strategies has increased the legitimacy of China at a regional level, for example, with ASEAN+3 or the Shanghai Cooperation Organization. According to the words of Xi, it is possible to have a clear understanding of how China is willing to reform the international system, going beyond the world order dominated by the West. The new China-led initiatives and organizations, i.e., the BRI and the AIIB, are deeply connected to the CCP ideational narrative in global politics. In more detail, there can be unraveled precise ideational origins behind the newly designed initiatives. The Fifth Generation of Leaders has developed new concepts such as China Dream, a New Type of Great Power Relations and a New Type of International Institutions. In this regard, China cannot be portrayed according to the international political thinking that conceives its rise to be inhibited or deflected<sup>38</sup>. China is becoming a proactive player in the global order, and with the advent of Xi Jinping coming to power in November 2012, Chinese foreign policy has changed according to the main priorities of the country. The Chinese president has fostered the idea of *奋发有为 (fenfa you wei)* striving for achievements. Moreover,

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<sup>38</sup> Dian (2017)

China's rise and the shift of the global order is generating opportunities that are in line with the leader's expectations<sup>39</sup>.

It is essential to underline that the visions of the world are different. On the one hand, Western powers have a universalistic approach to global governance, on the other hand, other countries such as China and Russia believe that context matters and the idea that in international politics each country should protect its political regime prevails<sup>40</sup>. As a consequence, this is why often Chinese proposals adhere to the Five Principles of Peaceful Co-existence which are the "principles of mutual respect's for territorial integrity and sovereignty, mutual non-aggression, mutual non-interference in each other's internal affairs, equality and cooperation for mutual benefit, and peaceful coexistence"<sup>41</sup>. These Five Principles of Peaceful Co-existence explain the willingness of China to commit to never seeking hegemony or expansionary acts. As a matter of fact, these principles govern state-to-state relations seeking a peaceful settlement of disputes pushing forward many regional and global initiatives such as the Shanghai Cooperation Organization and the Six-Party Talks regarding the Korean Peninsula issues' that have affected the international relations in the last decades. The peace and development of every country, especially in the Asia region are at China's heart and this is one of the reasons that pushed Beijing to establish the Belt and Road Initiative. The Chinese narrative is a product of both tradition and innovation, socialism with Chinese characteristics, and New Confucianism 新儒家(*xinrujia*). The latter is used in order to strengthen the awareness of the Chinese people and their prominent role in the world, which helps to emphasize peace and harmony.

One of the reasons for the success of China's new role in global governance can be detected in the attention that the country arose worldwide. The most important example is the concept of China Dream, which is a legacy of the past and is intertwined with another fundamental concept, i.e., the *Tianxia* system (all under heaven). Moreover, the idea of Xi Jinping to build a new type of international relations is at the core of China's foreign policy narrative and public diplomacy. The program for a new kind of international relations has to build win-win cooperation politically, economically, and

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<sup>39</sup> Breslin and Menegazzi (2017)

<sup>40</sup> Marchetti (2017)

<sup>41</sup> Xi (2017)

culturally also with a focus on security issues. So, the policies China will pursue in the next years will be the key not only for the country itself but also for other countries worldwide. The ability of China remains to find a balance between the Chinese interests in international affairs and the interests of other countries in this sphere.

This new vision was expressed during the 18th National Congress of the Communist Party of China (CPC), and it consisted in the idea of serving China's dream of national rejuvenation with peaceful development as the pathway. Moreover, the concept of developing socialism with Chinese characteristics was the original path to follow. The concept of building socialism with Chinese characteristics was first put forward by Deng Xiaoping which underlined the need for China to continue to pursue socialism by adapting Marxism to China's conditions, incorporating practice, theory, and system. This system is unique in its genre, and it has proven to be effective. The concepts as mentioned above, have been stressed recently during the 19th National Congress of the Communist Party of China, which has taken place in October 2017. The Congress pointed out the 14 points that should be followed and fulfilled in order to develop socialism with Chinese Characteristics in this historical juncture<sup>42</sup>. The 14 points concern and address the whole society, from the Party leadership to the people. Nation and Mankind are bound together, and success comes when they collaborate and cooperate in order to accomplish the same goal. Together they will reach the prosperous, secure, culturally advanced, harmonious and beautiful China. The concept of *Tianxia* (天下) is meaningful; under heaven, everyone should be one family, nation, and humankind are bound together.

China's advancement of "a new type of international relations" is related to the promotion of "a new type of international institutions." The new Chinese initiatives in regional economic governance and international cooperation are the result of Confucian ideas such as harmony, mutual benefit, and inclusiveness. The One Belt One Road initiative embeds the purposes mentioned above, and the AIIB is not presented as a new Chinese hegemonic tool to challenge global economic governance. On the contrary, it is a way to protect Asian developing countries vis-à-vis the interference of the Western-led international institutions.

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<sup>42</sup> Xinhua (2017)



The Chinese approach towards the international economic order has changed and it is different from the one of the past. According to the leader Deng Xiaoping – a supporter of the introduction of the reform and opening up in 1978 - China shares a common destiny with developing or Third World Countries; however, the main task is not to become a hegemon, but instead spread and defend peace<sup>43</sup>. China is not willing at all to subvert the existing world order by any means; on contrary China is trying to integrate itself in the global order promoting ideational resources.

### **2.3.1 The Chinese Dream**

From the founding of the PRC in 1949 and since Deng Xiaoping’s reform and opening up in 1978, China and Chinese society have experienced development and progress. In less than 40 years, the economy boosted and has become the second world largest economy achieving prosperity. This process had remarkable significance also in China’s contribution to world peace and development. China remains the world’s largest developing country. Many impoverished areas developed and achieved better living conditions and higher standards of living. To the goal of improving people’s living standards and achieving common prosperity Two Centenary Goals have been put forward. The first one regards GDP, and per capita income, which compared to 2010 levels should be doubled and then the building of a prosperous society by 2020 since the centenary of the CPC is approaching. The second concerns the building of a prosperous China in the context of a modern socialist country, which will be harmonious, culturally advanced and achieve the rejuvenation of the Chinese nation by the centenary of the PRC in 2049. All these reforms will have an impact on a deeper level, and besides, implementing the rule of law and running the Party with discipline is part of the Four-pronged Strategy. The Chinese Dream 中国梦 (*Zhōngguó Mèng*) is a concept that relies on the people’s dream and has at its heart the Chinese people’s aspiration for a better life. The AIIB can be considered as a tool, as a multilateral mechanism, an organization, that promotes and compliments Xi’s vision of the Chinese Dream. The Chinese Dream has not only a regional focus but also a world focus. All these “dreams” are supported by concrete

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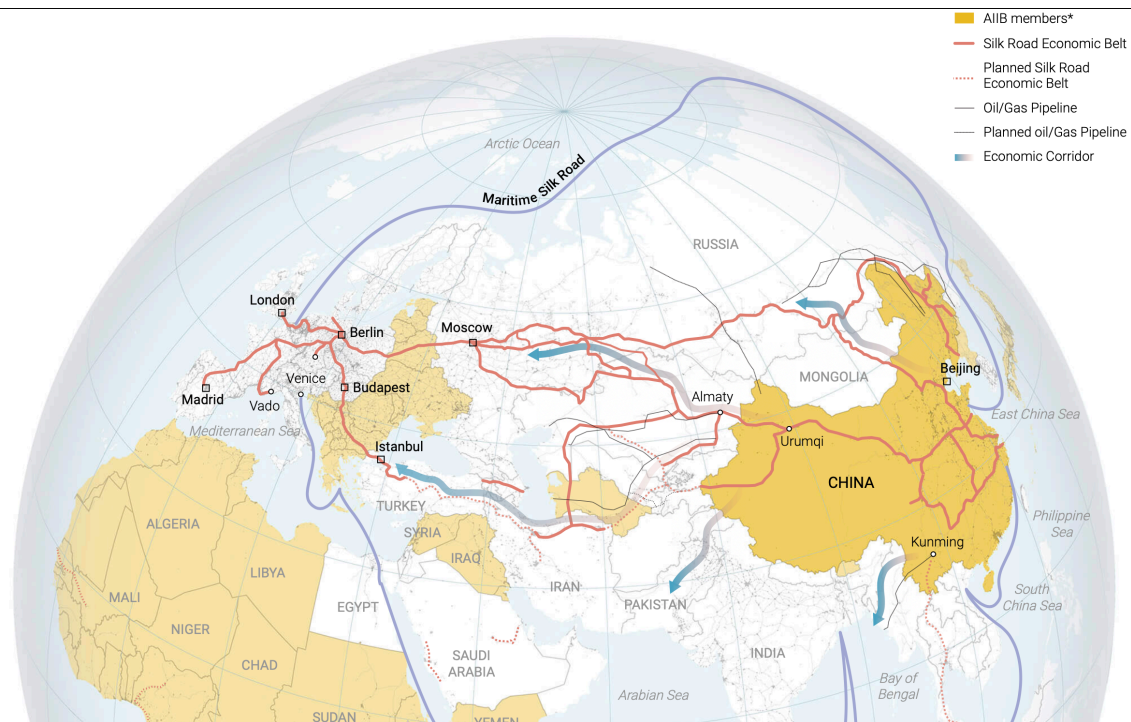
<sup>43</sup> Xi (2017)

projects and will help solve China's internal issues. The foreign policy has been shaped with a strong focus on the Chinese Dream and the One Belt, One Road strategy that combined with the establishment of the AIIB can fulfill Beijing's domestic and foreign policy goals.

## **2.4 The Belt and Road Initiative (BRI)**

Deng Xiaoping's blueprint became a reality. The Chinese Dream is coming true and tangible through hard work and commitment of the whole society for a better life. People are put at the center; living standards have changed, leading to remarkable overall changes.

The motivations behind the AIIB can be explained in the context of the One Belt One Road 一带一路 (*yidaiyilu*) or also called the Belt and Road Initiative which was born as an initiative to boost multilateralism, bringing win-win progress and cooperation. This is an opportunity to stimulate the economies of China and the countries involved in the BRI, such as Myanmar, Cambodia, Vietnam and so on. The motivations under this project lie in the guidelines of the new domestic and foreign policy objectives. It appears that Chinese strategic thinkers advocated a new strategy in order to counterbalance rising tensions in the Pacific region with the United States and Japan. Africa is benefitting from this cooperation with China through the aid of the latter to the former. The OBOR initiative, known as the Silk Road Economic Belt and the Twenty-first century Maritime Silk Road, was proposed by leader Xi Jinping during a visit in Kazakhstan and Indonesia in September and October 2013. It can be defined as a multi-level initiative of economic diplomacy. As it is shown in the figure, it includes Southeast Asia as well as Central Asia and West Asia (Fig.1). The initiative was part of China's 13th Five-Year plan, which started in 2016. Furthermore, contemporary to the OBOR the Chinese government has been promoting other regional initiatives such as the FTAAP: a trade deal which involves 21 economies part of the Asia-Pacific Economic Cooperation.



Source: South China Morning Post (2019)

Fig.1<sup>44</sup>

To give a brief overview of the ancient Silk Road, the Silk Road began with the Han Dynasty (206 BC – 220 AD). It was characterized by multiple exchanges of goods, for instance, gold, silk, tea, precious materials and so forth. It was a network of routes where merchants traded. At the beginning, these exchanges were happening on land routes, but when the Ming Dynasty came to power, maritime routes were preferred in particular for the transportation of fragile, precious materials such as ceramics. The new Silk Road follows the paths of the ancient one, however, now three land<sup>45</sup> routes and two maritime<sup>46</sup> routes have been established and consolidated.

The first China-led multilateral development Bank, the Asian Infrastructure Investment Bank (AIIB), was also announced in October 2013 when Xi Jinping highlighted the willingness to implement new policies related to the One Belt One Road initiative. According to the words of the leader Xi Jinping, the “primary task” of the newly

<sup>44</sup> Available at:

<https://multimedia.scmp.com/news/china/article/3007692/belt-and-road/index.html>

<sup>45</sup> The Northern Route: Beijing-Russia-Germany-Northern Europe. The Middle Route: Beijing-Xi'an-Urumqi-Kazakhstan-Hungary-Paris. The Southern route: Beijing-Kashi-Pakistan-Iran-Iraq-Turkey-Italy-Spain.

<sup>46</sup> From South China ports to the Indian Ocean, Africa, and Europe.

established Bank is to provide capital for the initiatives mentioned before <sup>47</sup>. Moreover, contemporary to the proposal of the AIIB, China has designed a new \$40 billion Silk Road Fund and introduced further supports to the initiative through \$31 billion in China's policy banks. In order to overcome the impediments to intra-regional trade such as transport costs and connectivity, new highways and railway networks were encouraged.

A meaningful example of the success of this China-led initiative is the process of modernization that Kenya is experiencing in these years. Rail travel was not possible in Kenya until China helped the country with a brand-new line. Infrastructure was needed in order to build a modern Kenya. One of the main tasks is to improve infrastructure in developing countries, whether trains or airports. The Chinese are investing all over the world and the BRI is meant to build massive infrastructure that will link China with Central Asia, West Asia, the Middle East and Europe, whereas the maritime Silk Road has the aim of bringing together Southeast Asia, the Indian Ocean, Oceania and as well parts of Africa (Fig. 1). The plan seems to be issued by the central government with a vast geographical scope which will invest US \$ 1 trillion in highways, railways, ports, energy, oil pipelines and projects regarding the extractive industry<sup>48</sup>. It will cover more than 70 countries that count for more than a half of the population of the world.

However, the main challenge will be to meet the conditions that need to be fulfilled regarding environmental sustainability and social goals, such as transparency and public debate. Many critics have arisen regarding the transparency of the projects. Western countries and policy-makers in Washington are concerned the BRI is a Chinese strategy to exert political influence serving to extend China's geopolitical reach on a global scale. Also, regarding the projects, strict conditions have been imposed on the borrowers, which will have to use only Chinese companies and technologies. Moreover, concerning the projects, many critics emphasize the so-called debt-trap diplomacy.

An important case of the mentioned debt-trap diplomacy involves China's engagement and financing in Sri Lanka. The port of Hambantota was under construction by China. Since it generated a lot of debt Sri Lanka and the country was not able to repay the debt, it was obliged to hand over the port and the land surrounding the port of Colombo for 99 years<sup>49</sup>. More widely speaking, this piece of land is an asset for China for its geostrategic purposes since it is near to the shores of India. There is an important

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<sup>47</sup> Xinhua (2015)

<sup>48</sup> Kuo and Kommenda (2018)

<sup>49</sup> Abi-Habib (2018)

aspect to be underlined, which is the market failure coming from a lack of financing in infrastructures. Another market failure is highlighted by low-income countries that were not able to repay the debt, so China has been criticized for debt sustainability. One of today's problems relies on the issue of debt sustainability and the Chinese have published a portfolio regarding the question of debt sustainability. Regarding the criticism the Ministry of Finance of the People's Republic of China has released on April 25, 2019 the "Debt Sustainability Framework for Participating Countries of The Belt and Road Initiative"<sup>50</sup>. China has lent capital to low-income countries with not many conditions, and these countries found themselves with high debts. The document sees a new position of China in evaluating debt-sustainability by applying the same criteria as the IMF and the World Bank. In this case date matters since the second and last Belt and Road Forum took place just some days before, and precisely on this occasion, China released the report.

The Silk Road will help invigorate the economies of Africa and Asia, and at the same time, it will stimulate the economies of Europe. Railways, roads and bridges, ports are under construction in developing countries such as Ethiopia.

China promotes the One Belt One Road as a win-win initiative, bringing overall global economic growth, one of the most critical worldwide initiatives so far that will bring prosperity and peace. The principles are in line with the purposes of the UN Charter and the Five Principles of Peaceful Coexistence. The philosophy brought by Xi Jinping is meant to bring a genuine sense of destiny. The leader has a good understanding of history, is far-sighted, and the concept of a community of shared destiny has deep resonances in the Chinese tradition. The shared destiny will benefit everybody. Globalization and the shared destiny are both present in a multilateral institution, the Asian Infrastructure Investment Bank. The ways of financing have been innovated. Facilities that could not be achieved by countries alone are improving the lives of everyone in the community, and through these initiatives, the global economy will be integrated. However, the implementation of these two initiatives will have a more significant implication in the world, since developing countries will recognize China's model of development, this will fulfill in the long-term Beijing's geo-economics and geopolitical strategic objectives.

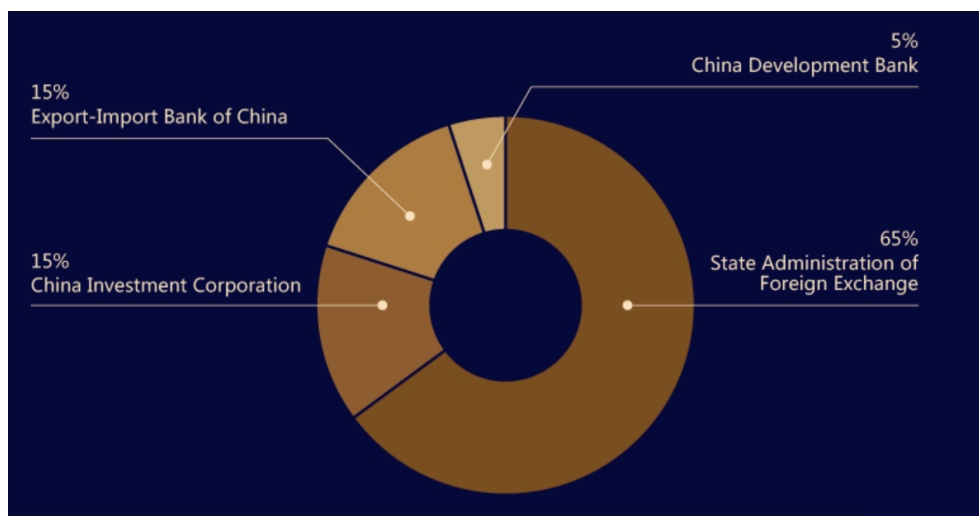
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<sup>50</sup> Ministry of Finance of the People's Republic of China (2019)

## 2.4.1 The Silk Road Fund

In this paragraph the Silk Road Fund is described since it is the major source of funding for the OBOR. The AIIB is complementary to the OBOR but it must be highlighted that it does not operate in projects related to the OBOR.

The Silk Road Fund was established in Beijing on December 29, 2014. The Fund was established in order to provide capital for the projects along the OBOR. It is a fund with strong investment from the State Administration of Foreign Exchange, China Investment Corporation, Export-Import Bank of China and China Development Bank. From now on defined as the Fund, it has the purpose of providing financing and investment support for trade and economic cooperation under the framework of the Silk Economic Belt and the 21<sup>st</sup> Century Maritime Silk Road Initiative<sup>51</sup>. Transportation, energy, and telecommunications are at the center of these initiatives.



Source: Silk Road Fund Website, 2019

Fig.2<sup>52</sup>

According to the shareholder structure (Fig.2), the Fund has a total capital of US \$40 billion and RMB 100 billion. The capital distribution is committed by the State Administration of Foreign Exchange of 65%, the China Investment Corporation of 15%, the Export-Import Bank of China of 15%, and the China Development Bank of 5%.

<sup>51</sup> Silk Road Fund website (2019)

<sup>52</sup> Available at: <http://www.silkroadfund.com.cn/enweb/23775/23767/index.html>

Moreover, the Fund follows the philosophy of openness, inclusiveness, and mutual benefit. It has engaged with multilateral institutions and platforms, and among them, it includes the International Finance Corporation of the World Bank Group, the European Investment Bank, and the European Bank for Reconstruction and Development.

The Fund follows universal international standards and norms, China's laws and regulations and the ones of hosting countries. It works actively in order to pursue high environmental standards and addresses its social responsibilities. The Corporate Governance is structured with a Board of Directors, a Board of Supervisors and Senior Management.

## **2.5 The launch of the Asian Infrastructure Investment Bank**

In 2012 a new way of having relations with the Asia Continent and the rest of the world had been developed. The reasons behind the creation of the AIIB can be detected in a reorientation of Chinese foreign economic policy that took place with the advent of Xi Jinping becoming the General Secretary of the Chinese Communist Party in 2012 and then president in 2013. Opposed to his predecessor Hu Jintao, Xi Jinping started a new agenda pursuing new neighboring diplomacy based on the aim of building deeper economic, security and political ties. The so-called "Chinese Dream" vision started to be regional and global, shifting the focus from the national one. A foster in regional development and credibility is needed in order to be in line with the Chinese view of "harmonious world."

Moreover, an increased interest in the Asia-Pacific area was underlined by the geopolitical and economic importance of this area to China. China has signaled the capacity of providing International Development Finance (IDF). In the 13th Five Year Plan, new guidelines over a new way of development called "new normal" have been introduced to face internal issues. Concerning the AIIB initiative, this came from Chinese president Xi Jinping, an ambitious leader which has acquired power from when he came to the stage. The book in which all his thoughts and plans are collected is *The Governance of China*, it was issued in October 2014, and it has been translated into several foreign languages. His ideas reflect the strong leader and rising China.

As a consequence of this new leadership, new policies have been required. During Xi's leadership, new terms have been introduced, such as "Chinese Dream," "harmony," "new normal," and "better world". These concepts are considered as guidelines not only at a national level but also at a global one. The Chinese government under Xi Jinping is trying to address domestic problems and challenges and seeks a more significant influence in the world. Besides, many developed countries chose to join the bank and perceived investing in Asian infrastructure through the AIIB as an opportunity instead of a threat, constituting "a coalition of actors" that is not antagonist towards the status quo. The OBOR consists of land and maritime routes to develop the Asian region.

Moreover, it will create a series of routes for goods, services, energy, and other assets from China to Europe. The AIIB is the provider for stability and infrastructure development in the region. Furthermore, it is a new type of international financial institution (*以一个新型的国际金融机构 yi ge xinxing de guoji jinrong jigou*) the second multilateral development Bank founded since the European Bank for Reconstruction and Development in 1991.

President Xi and Premier Li Keqiang addressed the project of the AIIB in 2013 during their visit to Southeast Asia. From that moment, the shaping of the Bank started to develop.

In October 2014 representatives from 22 countries signed the Memorandum of Understanding (MOU) to establish not only the Asian Infrastructure Investment Bank but also the headquarters of the Bank which are located in Beijing. Mr. Jin Liqun was appointed as the Secretary-General of the Multilateral Interim Secretariat. The Secretariat was tasked to perform technical preparations for the purpose of the AIIB and to provide technical support and services for the Chief Negotiators' Meetings. The Prospective Founding Members established a forum, the Chief Negotiators Meeting (CNM) in order to negotiate and agree on AIIB's Articles of Agreement and other issues related to the Bank's establishment. Five Chief Negotiators Meeting took place before the Bank started its operations. The first CNM was held in November 2014 in Kunming, China. A second CNM took place in Mumbai, India in January 2015 and in that occasion, discussions were open for the drafting of the Articles of Agreement. A third CNM followed it in Almaty, Kazakhstan in March 2015. March 31 was established as the deadline for the submission of membership applications, in the meantime, the number of Prospective Founding Members had increased to 57, and the 4th CNM was organized in Beijing in April 2015.



The final text of the Articles of Agreement was adopted in Singapore during the last Chief Negotiators Meeting on May 22, 2015. The Articles were signed by all 57 PFMs in the second part of the year, between June 29, 2015, and December 31, 2015.

The Articles entered into force on the 25th December 2015, and 17 Signatories have deposited instruments of ratifications. According to the Articles of Agreement, Article 1 describes the purposes of the Bank which shall be to:

“(i) foster sustainable economic development, create wealth and improve infrastructure connectivity in Asia by investing in infrastructure and other productive sectors;

(ii) promote regional cooperation and partnership in addressing development challenges by working in close collaboration with other multilateral and bilateral development institutions”<sup>53</sup>.

AIIB’s role is to promote investment in the region and to prioritize the needs of less developed members; however, it does not have as the main objective to reduce poverty. The Bank was established with a capital base of US\$100.000.000. The structure of the Bank is not different from the Asian Development Bank or the World Bank. However, the AIIB was part of a more significant project, the OBOR initiative. The OBOR initiative, known as the Silk Road Economic Belt and the Twenty-first century Maritime Silk Road, was proposed by leader Xi Jinping during a visit in Kazakhstan and Indonesia in September and October 2013. According to David Dollar<sup>54</sup>, a former World Bank employee and currently advisor of the Chinese government over the AIIB, the Bank will be the most critical financial and institutional mechanism for implementing the OBOR strategy.

The initiative was also part of China’s 13th Five-Year plan, which started in 2016. The Asian Infrastructure Investment Bank aims to foster connectivity and help develop infrastructure in member states which are not able to meet the infrastructural challenges in Asia. Some writers portray the AIIB as consistent with the Chinese political economy and the China model, which presents “a system of authoritarianism combined with

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<sup>53</sup> AIIB AOA art. 1

<sup>54</sup> Dollar (2015)

increasing market-oriented economic activities, making it different from virtually all other great powers”<sup>55</sup>. The AIIB suits the overall Chinese strategy, and now that China has evolved into a global economic power, there is more concern of domestic and international players in its decision-making. Different from the United States and the rest of the world, the Chinese political-economic system is unique. As a matter of fact, the Chinese system is a hybrid one, which is compatible with the global financial system, and since the China model is a hybrid one, the AIIB follows this model. Moreover, the AIIB borrows the experience of the World Bank and ADB since many former World Bank and ADB employees’ have been advising the Chinese government over the AIIB.

The AIIB was officially launched in January 2016 after 27 months of preparation. Notwithstanding the good Chinese intentions to build through development, mutual respect, and win-win cooperation, the AIIB was initially seen more of a challenge. However, after more than two years of operations, it managed to affirm in the international arena also being backed and financially supported by western founding members. The membership has risen from the announcement in 2013 to these days. The growing number of members is a positive achievement for the China-proposed Bank. Not only developing countries participated in the initiative but also developed countries from Europe. This positive outcome has attracted more countries from the beginning, although some US pressures have risen, especially toward the UK, which was the first European country to adhere to the initiative.

### **2.5.1 How the Bank works**

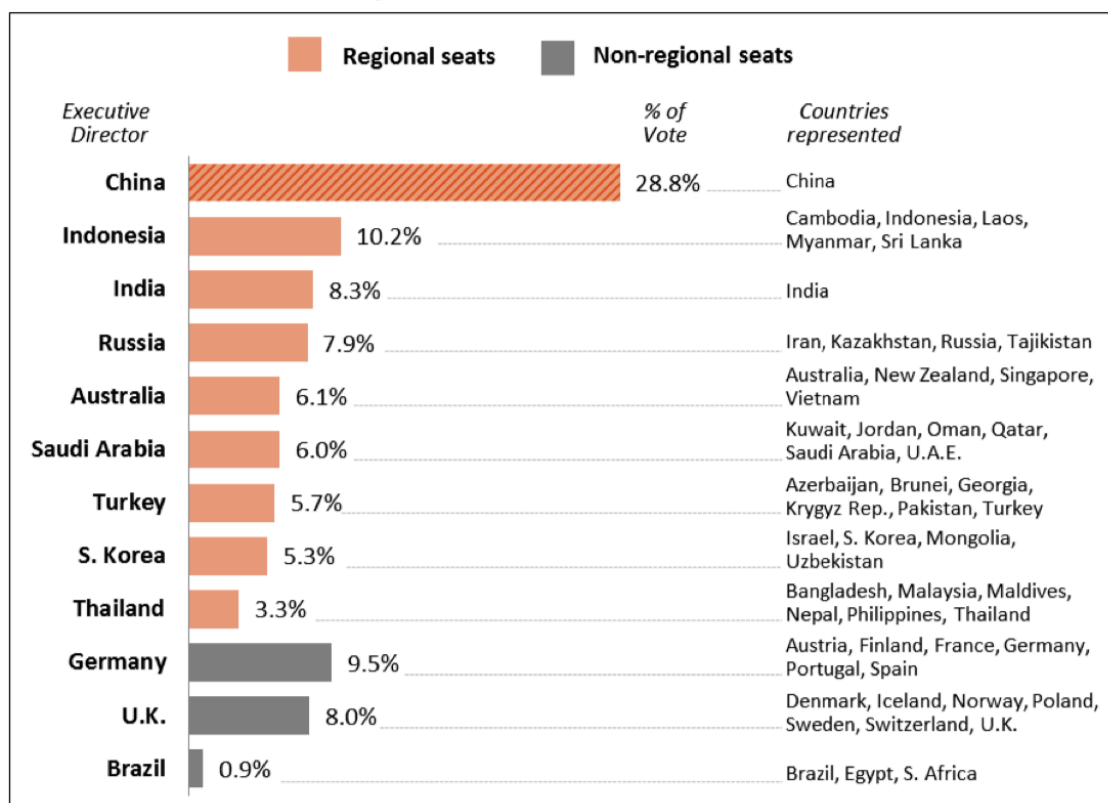
The governance of the AIIB comprises a Board of Governors, a Board of Directors and a Senior Management Board. Articles 21-31 of the AOA define the governance structure of the AIIB. The decision-making sees the Board of Governors as the highest organ. Two governors, a governor, and an alternate governor, are designated in order to represent each member country. Many functions are performed, from the admission and the suspension of members to the President’s election and amendments on the Articles of Agreement or changes to the composition of the Board of Directors. The organ just mentioned meet at least once a year, and it is non-resident, which means that members

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<sup>55</sup> Wan (2016)

of the Board of Directors and Board of Governors can make decisions in home countries. The Board of Governors is in charge of establishing major policies of the Bank, approving the annual plan, strategy and the budget of the Bank<sup>56</sup>.

**Figure 3. AIIB Board of Directors**



Source: AIIB, CRS.

Source: AIIB, CRS as of 2017

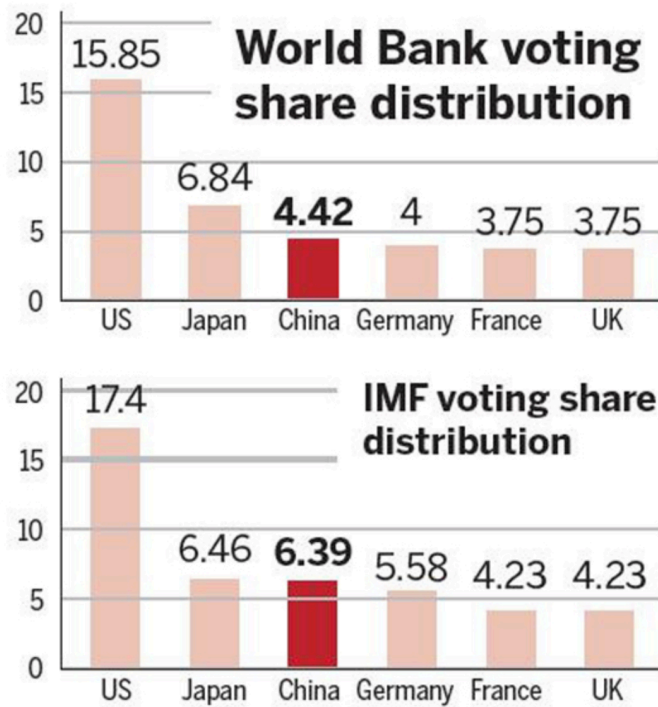
Fig.3<sup>57</sup>

According to the Board of Directors, voting rights, the main stakeholder in the AIIB is China, with 28.8% of the voting rights. There is a significant gap in the voting rights between China and the other stakeholders. India and Russia hold 8.3% and 7.9% respectively. The constituency of Indonesia, Cambodia, Myanmar, and Sri Lanka hold together one-third of Beijing voting rights. However, if we look at the US voting rights in the World Bank and the IMF, the situation is similar. This figure is updated to 2017, now as of June 10, 2019, the constituency of non-regional countries has more members

<sup>56</sup> AIIB AOA Article 16

<sup>57</sup> Available at: <https://fas.org/sgp/crs/row/R44754.pdf>

(Cyprus, Ireland, Italy, Luxembourg, Malta and the Netherlands). Besides, this constituency appointed Austria and since it is based on rotation the next will be France.



Sources: World Bank, IMF, graphics by China Daily (2017)

Fig. 4<sup>58</sup>

The US holds 17.4% of the voting rights in the IMF and 15.85% in the World Bank after the reform. Beijing also has a consolidate majority in the Board of Directors of the AIIB.

Since many projects approved by the Bank can have an impact on social issues, the AIIB adopted its Project-Affected People’s Mechanism (PPM) following other MDBs. In 1993 the Inspection Panel was first established by the World Bank, namely the independent accountability mechanism (IAM). The idea did not come out from the blue,

<sup>58</sup> Available at : [http://www.chinadaily.com.cn/business/2017wef/2017-01/16/content\\_27965250\\_8.htm](http://www.chinadaily.com.cn/business/2017wef/2017-01/16/content_27965250_8.htm)

but since many large-scale investments, such as the Sardar Sarovar dams in India, failed in properly considering the impacts of these on local communities. IAMs is a valuable instrument to bring the voices of people who may suffer harm to express their concerns regarding the feasibility of a project in paying attention to environmental and social issues.

Following the path of the World Bank and in order to meet the international best practice, the AIIB also adopted its own “Project-Affected People’s Mechanism” (PPM) in December 2018<sup>59</sup>. The PPM is to be effective as of 31 March 2019. However, the risk of a downward spiral is underway. The World Bank’s Environmental and Social Framework, effective in October 2018, is in many regards similar to the AIIB’s ESF. The authors served both the WB and the AIIB; and this is also why they are similar. More importantly since the AIIB is based on “no strings attached” loans from Chinese banks, there is a probability of downward requirements on environment and good governance, which is likely to deter clients from World Bank’s loans<sup>60</sup>. For instance, India chose to join the AIIB in particular for this policy.

Whether the AIIB can improve sustainability in Asia is another major issue. According to the official documents released on the Environmental and Social Framework (ESF)<sup>61</sup> the China-led Bank is reinforcing the existing sustainability norms and President Jin Liqun has always pointed out the robust ethical standards which are transparency, integrity, sustainable development, and accountability. The concept of sustainability is a core principle, underlined in the Articles of Agreement with the support of the Board of Directors. The ESF is aligned with the one of existing MDBs, and the AIIB firmly establishes itself as a status quo financial institution while improving sustainability norms. And this goes in hand with China’s interest to enhance its legitimacy and good reputation not only in the Asia-Pacific region but also worldwide. China’s commitment to infrastructure development complements other MDBs, and it is not likely to be considered as a challenger. With no doubt, it leads to a situation of competitive pluralism, but it is based on healthy competition, which in the best case can lead to new and innovative policies within the framework of the development world.

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<sup>59</sup> AIIB (2018)

<sup>60</sup> Horta (2019)

<sup>61</sup> AIIB (2016)

The AIIB has the potential of becoming in the long-term an advocate of sustainable development, and the international community should be welcoming.

Besides, the Bank presents a new opportunity for exchanging knowledge between advanced and emerging economies and provide new global goods. Moreover, the AIIB as an institution has steadily advocated for the United Nations 2030 Sustainability Agenda. Furthermore, under the circumstances, China is promoting its interests through economic diplomacy as a soft power tool in order to develop a good neighboring diplomacy<sup>62</sup>.

Moreover, on the day of the first annual meeting, it was also approved the implementation of a Special Fund for the preparation of projects, and China contributed to the Fund with \$50 million. Regarding the Senior Management Board, this organ has the President and Vice Presidents. So, the most significant innovation of the AIIB lies in the governance structure. The two boards are non-resident and unpaid, and there is less red tape than the other MDBs. English is the working language of the Bank. The first AIIB Business and Budget Plan was released on January 16, 2016. The first activities amounted to \$52.4 million for administrative costs and \$7,5 million dollars as resources of capital. From the beginning, a highly qualified working staff has been appointed, a strong ethic based on the values spread by the Bank, and in order to build up high-quality investments, a platform was activated. Concerning the decision-making of the Bank on approved projects, there is a problem regarding the choice of recipient countries for investments. Article 11, point 1, sub-paragraph a, “Recipients and Methods of Operations” specifies as for recipients that “ the Bank may provide or facilitate financing to any member, agency, political subdivision or enterprise operating in the territory of a member or concerned with the territory of the region”<sup>63</sup>. The article is not specific enough, and this leads to an adverse selection operated by the Bank. Besides, many criticisms were made to this kind of process for selecting the recipient countries, and the AIIB published a new *modus operandi* following the origination principle of the WB. At the time of this writing, 38 projects have been approved by the Bank. Although the majority of the projects are co-financed with other MDBs (WB, EBRD, ADB), such projects will be complementary to the BRI. The largest shareholder is China, which has contributed with

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<sup>62</sup> Hanlon (2017)

<sup>63</sup> AIIB AOA Article 11, point 1, sub-paragraph a

\$29.78 billion, and according to the Articles has a *de facto* veto power on decisions that require a 75% supermajority. Among the main contributors to the Bank, India, Russia, and South Korea, are regional countries from the Asia-Pacific region, and outside the region, we find the largest contributors are Germany, France, and Brazil.

Article 31 of the AOA stresses the conditions that all members should follow in order to be part of the new project. Political sovereignty and non-interference are much emphasized:

“The Bank, its President, officers and staff shall not interfere in the political affairs of any member, nor shall they be influenced in their decisions by the political character of the member concerned. Only economic considerations shall be relevant to their decisions. Such considerations shall be weighed impartially in order to achieve and carry out the purpose of the Bank”<sup>64</sup>.

Mechanisms have been activated for the facilitation of the entrance of the private sector in financing infrastructures. Investors are increasingly participating in the infrastructure sector. In particular, in multilateral scenarios, investors are keener to participate in projects, which involve the financing of infrastructures, in partnership with Multilateral Development Banks such as the World Bank.

There are several difficulties in financing infrastructural projects as they absorb a lot of resources, time, and are risky, especially for the low GDP countries. Often the low GDP countries cannot repay the loans in a sufficient amount of time.

The AIIB loan selection model was slightly different from the one of the World Bank and has been criticized. While both the World Bank and the AIIB apply the principle of origination to assess which projects they finance, the AIIB has different assessment criteria. The World Bank has more stipulations in place for a country that receives a loan while the AIIB is more lenient. The AIIB was funding projects, but the quality of the projects presented were not following high standards. In order to combat criticisms, the AIIB worked together with seven other MDBs, including the World Bank, EIB, EBRD, ADB, and the Inter-American Development Bank, to create new standards and policies for financial and economic review of loan applications, AKA the MCDF. The Multilateral Cooperation Center for Development Finance was announced on March 25, 2019 to help deliver higher quality projects by improving transparency and setting higher standards through an in-depth cost-benefit analysis. According to expert Joachim von Amsberg, VP

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<sup>64</sup> AIIB AOA Article 31

specializing in policy and strategy of the AIIB, “We analyze whether the finances of the project are sound and whether the project generates the revenue necessary to pay back the loan; we analyze the economic impact of the project, making sure that it's a good project for the country”<sup>65</sup>. By entering into this “Memorandum of Understanding” (MOU), the AIIB has shown its willingness to provide transparency into its loan process and ensure they are making wise decisions when evaluating applications. This supports the notion that the AIIB is contributing value to the global financial markets by playing nice with the other MDBs of the world.

Now let’s discuss the primary objectives of the AIIB according to their bylaws. One of the main objectives of AIIB is financing infrastructure projects, but not to finance the project entirely, but to encourage private investment as well. They are using sound economic principles like diversification of the investment portfolio or creating bonds to attract private capital<sup>66</sup>.

Furthermore, on the topic of bonds, the AIIB recently released S&P and Moody’s triple-A rated bonds into the market to encourage infrastructure investment. These bonds, issued May 9, 2019, mark a major achievement for the bank, highlighting their dedication to enhanced transparency and accountability. “AIIB is committed to best practices and modern risk management; and it has implemented an economic capital and stress test policy framework to manage its capital”<sup>67</sup>. This is the same bond rating of the United States Treasury bonds and the World Bank bonds. It is a milestone for the Bank, considering that it is a startup and yet not well known worldwide. This illustrates how they are trying to operate within the global standards and make themselves known legitimately. While its unknown their long-term impact, we can see in the short term that the AIIB has contributed positively to the world stage of finance.

How the AIIB can improve and change the financial architecture is still too early to be predicted. The World Bank, for instance, changed the Bretton Woods mandate after 40 years. Only in the 1980s, there has been a change after the mandate of reconstruction was accomplished, as a matter of fact, the WB changed the focus focusing on the reduction of poverty.

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<sup>65</sup> Zhang (2019)

<sup>66</sup> Suokas (2018)

<sup>67</sup> AIIB (2019)



# **Chapter 3 How Regional and Non-Regional Actors Responded?**

## **3.1 Why Regional and Non-Regional Members welcomed the AIIB?**

In 2015, fourteen of the 28 EU states became founder members of the Bank. Not only significant players such as the UK, France, and Germany, but also smaller states such as Denmark, Luxembourg, and Malta decided to take part in the initiative. Following the EU member countries response to the project also some NATO members joined the AIIB. Only Germany and France, major players in NATO after the US, adhered to the initiative despite the contrary opinion of the US. The United States and Japan are both absent since they perceived the project as a loss of power from their perspectives. Although the initial proposal was to prioritize the Association of Southeast Asian region (ASEAN) member countries to foster ties and deepen connectivity between China and ASEAN economies, later Xi Jinping highlighted the willingness to include as many countries as possible from three continents: Asia, Africa, and Europe. The consensus has not been unanimous; however, the success has been widely accepted, and many explanations can be outlined. Three lines of arguments can explain the perspectives of joining countries. Firstly, forming and joining an international institution can provide multiple benefits. It can provide legal liability, reduce transaction costs, reduce uncertainty and information-asymmetries. As a matter of fact, European members can expect to experience economic benefits and have access to broader investment markets and build stronger relationships with Asian states.

The second argument is based on the negative realist perspective on international institutions. According to realists' scholars, international institutions do not work properly and are not able to address the discrepancies since the world is an anarchic one. In the triangle between the USA, China, and a European country, the European countries decision will be greatly influenced by their relationship with the US mainly because they value their relationship and they don't want to create tension with an historical and powerful alliance.

The third explanation argues that international organizations can address both interest and power through formal and informal governance. And according to Renard<sup>68</sup>, the expectation coming from the European countries' side is that by joining the AIIB they will be able to promote a reform agenda and make sure that the bank will adopt the best practice in international development finance. Consequently, it appears that being a member of the AIIB will give the possibility to exert some informal influence on Chinese policies. If a country has good ties with China, then it will more likely be willing to join the Bank, vice versa if the relations between the two countries are not cordial then the country will have little reason to potentially risk weakening the strategic relations with Washington.

Moreover, according to Dittmer<sup>69</sup>, if the previous triangle China-Europe-USA can be conceptualized as a stable marriage, in which the USA and Europe were both hostile to China, now the structure has moved toward a romantic triangle, in which Europe may evolve and become a pivotal player.

To sum up, the findings show that wealthier European countries have more interest in becoming members of the AIIB and the cases as mentioned above, show evidence on this. Although the AIIB's governance standard is in line with those of the World Bank and ADB, Europe will monitor and push for reforms on the Bank's operations. Beijing should instead address Europe's strategic concerns, not only investment in infrastructure but also emphasizing trade opportunities that can come out from the Bank's projects. One of the central countries absent in its members is the US, which has started the creation of the post-World War II scenario. Not only it has driven the creation of the post-war international institutions, but it also has always been the main actor to operate within them.

As a consequence, China is the new leading player within the AIIB. Besides, we can also see the membership to the young Bank of non-regional members such as Brazil and South Africa, which together with China, India, and Russia form the BRICS which are considered to be fast growing economies. BRICS countries have launched their own MDB, the New Development Bank, at the same time as the launch of the AIIB. But leaving the BRICS countries aside, what is interesting is why the European Countries have decided to join the Bank since the EU has nothing in common with the AIIB.

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<sup>68</sup> Renard (2015)

<sup>69</sup> Dittmer (1981)

Another aspect that has to be highlighted is the lack of common foreign policy of the EU, there has been no coordination, and European Countries mainly followed the UK decision. Besides, major EU countries are the most developed worldwide and have already played a massive role in financing and ruling the pre-existing MDBs.

Most countries are part of the Organization for Economic and Cooperation Development (OECD), and in the preliminary discussions at the initial negotiations, OECD members were given the possibility to influence its rules and procedures, especially the principles of economic and social well-being that have been reused. According to this result, the AIIB is the product of both western and Chinese principles of cooperation and development. This feature can also be found through the words of President Jin, in December 2015 during the negotiations. From his words, it emerges the participation from all the shareholders to create something new but at the same time something based on sound principles and with an efficient government structure. The involvement of both developing and developed countries since the early stages of the AIIB represents a new forum for constructive discussions, bringing all the countries together in one institution. Moreover, the collaboration between two different groups of countries, the developed and non-developed ones, can represent a good start for an international framework that seeks reforms.

Despite earlier hesitations to joining the AIIB, Australia and South Korea have both joined as member countries of the AIIB, illustrating a shift in global financial institutions.

The young Bank has achieved significant progress and reached the expected milestones within the first years of cooperation. It was officially launched in January 2016 after 27 months of preparation. Notwithstanding the good Chinese intentions to build something new based on development, mutual respect, and win-win cooperation, the AIIB was initially seen more of a challenge. However, after more than two years of operations, it managed to affirm in the international arena also being backed and financially supported by western founding members. About 75% of the voting shares are allocated to Asia-Pacific countries so that developing countries have more voices in the Bank. 37 of 57 prospective members come from the region. The membership has risen from 57 to -at the time of writing- 97, including both regional and non-regional countries, developing and developed ones. The growing number of members is a positive achievement for the China-proposed Bank. Not only developing countries participated in the initiative but also developed countries from Europe. Another factor ensures more

degree of influence from European and other countries, of the 12-member board of directors, about 30% went to non-regional members. This positive outcome has attracted more countries from the beginning, although some US pressures have risen, especially toward the UK. In 2017, AIIB received top-notch ratings from three major global credit rating agencies, Moody's, Standard and Poor's, and Fitch. The AIIB was rated AAA in international capital markets. Also, through the support of all its members, the Bank aims to become a lean, clean, and green development bank for this century. Anti-corruption rules are one of the main pillars of the Bank. A "zero-risk" rating is promoting economic development by enhancing economic cooperation and assistance with neighboring western countries.

### **3.1.1 The Case of India**

China and India are two countries which have experienced different destinies under the influence of western powers. Today this is still visible, while India still suffers from poverty issues and in the past depended heavily on other powers, China is experiencing an ongoing economic boom which has started in the past century. They both are emerging powers with emerging markets, and they have a large share of the world population.

The relationship between India and China will be one of the most significant in the 21st century. Their relationship will also decide the future of global governance. Besides, their ability to cooperate will be pivotal on international issues ranging from climate change to multilateral negotiations. Some border issues have marked the relationship between the two countries in 1962, and the border war led India to view its neighbor with suspicion. The short battle at the foothills of the Himalayas with the defeat of the Indian's troops led to difficult relations. India gained independence from the United Kingdom only in 1947, and since then the country tried to grow, implementing domestic policies and pursuing neighboring diplomacy. However, India pursued economic growth differently than China. After Deng Xiaoping started the period of reform, China seemed to be destined for great-power status. While on the one hand, China was heading toward economic modernity and global recognition, India was still linked to the past with a "feudal" caste-ridden society, trying to get rid of the legacy of British imperialism. In recent years, however, the leaders of the countries, Chinese President Xi

Jinping and Indian Prime Minister Narendra Modi have tried to upgrade the Sino-Indian relationship.

India's increasing global role through the BRICS group and the G20 has become more prominent. Beijing and New Dehli are both aware and wary of Western-dominated international institutions, and India has backed China's efforts to build alternatives i.e., the Asian Infrastructure Investment Bank, the BRICS Bank, and the Shanghai Cooperation Organization. Economic exchanges between the two countries are growing. Chinese companies are willing to invest in India and the other way around. However, economic relations remain unbalanced. India runs a \$37.8 billion trade deficit with China and exports are mainly composed of raw materials than finished goods. The Presidents of the two countries are aware of the potential of the Sino-Indian relations, and they are committed to improving their ties through economic exchanges and people-to-people contact <sup>70</sup>.

India is not a member of China's Belt and Road Initiative yet, however, New Delhi is participating in the AIIB and signed up to be a founding member of it in 2014. Today India is the most frequent recipient country of infrastructure projects from the Bank and the second largest shareholding in the Bank after China. In a speech delivered in 2016 by the former Indian Foreign Secretary S. Jaishankar, the reasons behind the adherence of India to the AIIB but not to other BRI projects were explained with his words "All these endeavors feed into the changing connectivity scenario in Asia. The interactive dynamic between strategic interests and connectivity initiatives – a universal proposition – is on particular display in our continent. The key issue is whether we will build our connectivity through consultative processes or more unilateral decisions. Our preference is for the former, and the record bears this out quite clearly. Wherever that option is on the table, as most recently it did in the AIIB, we have responded positively"<sup>71</sup>. India has infrastructure needs that can be addressed by the AIIB which already is conceived as a valuable source to fill the infrastructure gap.

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<sup>70</sup> Martin (2015)

<sup>71</sup> Ankit (2018)

Moreover, another reason why India decided to join the AIIB, was linked to the fact that the World Bank in 2013 imposed rules and restrictions on loans for projects with a substantial ecological impact. India is still a developing country and an emerging economy which relies on coal. For this reason, many projects proposed to the WB could have been rejected. Indian authorities criticized the conditions regarding the rules imposed by the WB and will instead be looking to the AIIB for 100 billion USD in loans for coal energy projects<sup>72</sup>. In this regard, the AIIB can prove to be the ingredient that complements the other financial institutions and fills the gap whenever it is possible.

### **3.1.2 The Case of the UK**

Despite US pressures, the United Kingdom decided to join the AIIB as a founding member in 2015. Among countries that form the G7 (Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States), the UK was the first country to join the AIIB. The adherence of both developing and developed countries to the AIIB was a factor of success for the new Bank. The Chancellor of the Exchequer for the UK, Philip Hammond, has expressed the strong support the UK will give to the AIIB' mission to address the infrastructure gap that currently affects Asia. The UK would contribute \$50 million to AIIB's Project Preparation Special Fund. Moreover, the UK is actively influencing the AIIB from the inside, contributing with expertise and technical assistance.

It is essential to understand why the UK despite US pressures joined the Bank; therefore, I decided also to interview the First Secretary of Financial Policy from the British Embassy in Beijing on April 20, 2019<sup>73</sup>. The interview will be reported according to his words.

*“Why did the UK join the AIIB? Mostly because George Osborne, the previous Chancellor of the Exchequer, is very supportive of the China-UK relationship and he saw*

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<sup>72</sup> Chin (2016)

<sup>73</sup> The author interviewed Mr. Rhys-Gordon-Jones, First Secretary of Financial Policy of the British Embassy in Beijing, for the purpose of this work

*that a huge amount of value in positive engagement with China to try both to influence China for the better and also as a way of enhancing collaboration on economic matters. He was a real China advocate and he was interested in an economically financial dialogue, primarily an economic dialogue between the two countries and it was led by him along with vice premier Mark Carney at the time and then he would involve a whole host of different government departments so not to purely catch on Treasury related issues but also including a catch on government issues that regard economic science and innovation, trade, even agriculture, particularly infrastructure. He saw China's frustration with the Bretton Woods institutions and was interested in supporting China to help work through those frustrations and see how the UK could be supportive in financial flows and investment. When he first heard about the Asian Infrastructure Investment Bank, his instinct was to be supportive and, in a way, that he would help work with other institutions.*

*Moreover, only if the UK could have used its influence to help shape it, to make sure that it had high standards, to make sure that it was prone to good governance; if not, UK would not have taken part in this. Also being [that] the UK the first member to join it, it would go on diplomatic benefits with that as well. The primary driver should be a positive engagement to help influence from the inside so that it would have been additive to the global rule-based international system, able to contribute to enhancing international development in a way that was clean, following anti-corruption rules, environmentally liable, with good social standards and a global best practice. Frankly MDB's are pretty slow, and they take ages to approve projects, there is a lot of bureaucracy that not always help in a fast, effective way, [so] there are opportunities where the AIIB can add expertise”<sup>74</sup>.*

UK and China have a golden era. Several years ago, during a visit to the UK, the Prime Minister David Cameron and the President of the PRC agreed to have a golden era of relations on economic and financial matters, that's when the UK saw China's investments. The Chancellor of the Exchequer was in Beijing for the Belt and Road Forum to attend the Special Envoy of the Secretary-General and he had a long meeting with his new counterpart of the economic and financial department which is Vice Premier

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<sup>74</sup> The author interviewed Mr. Rhys-Gordon-Jones, First Secretary of Financial Policy of the British Embassy in Beijing, for the purpose of this work

Hu Chunhua. New days on the economic and financial dialogue are going to be held on June 17, 2019. Moreover, regarding the relationship between the UK and China, Mr. Gordon-Jones pointed out that the UK can help China and that their financial cooperation is crucial.

*“The relationship is good, as you have seen from the previous restorations of the FTAs, the UK has always been in advance with other major countries when it comes to financial cooperation in particular, and China is very keen to use the city of London as an internationalization of its economy, of its currency, of its institutions. The UK also has a major financial center that can help China to widen its network”<sup>75</sup>.*

Regarding the UK’s role in the AIIB there a couple of things to underline, one is that UK is a shareholder of the AIIB and is also going to be the first country in the world to contribute to the AIIB’s Special Fund. The Special Fund is a technical assistance facility that will help on project preparation, how to get infrastructure projects into place when they can reach financial and private capital, as well as Multilateral Development Bank capital, so it is as a way through the AIIB to take infrastructure projects and make them effective according to best practice and standards. Particularly from an environmental and social perspective, the UK helps ensure that the infrastructure is going to contribute to economic development that will be sustainable in the long term to widen sustainability. The Special Fund is something on which the UK has invested in both from a commercial and a sustainable point of view; South Koreans are also now participants to there is hope that that will help contribute to infrastructure progress in the future. The AIIB is a startup, it’s a new organization, MDB’s are complicated, they take time, the AIIB was quite slow to get funding out, it took a long time to think the internal organization, the recruitment of right people, assistance and processes, all of this has been designed from scratch. That is an incredibly difficult process, and other MDB’s are also co-lending the Bank. Regarding multilateralism, this is not just a Chinese institution to develop the Belt and Road, that is why it has a larger area of focus.

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<sup>75</sup> The author interviewed Mr. Rhys-Gordon-Jones, First Secretary of Financial Policy of the British Embassy in Beijing, for the purpose of this work



Another way the UK believes it can be influential in the AIIB is supporting sustainable infrastructure projects by coal reduction policies because they have a strong commitment to coal reduction. India is the largest recipient of funding; it has huge investment needs in particular in the energy sector and is still benefitting from the AIIB, although it is not part of the OBOR initiative. The UK is not advocating for coal; the country is leading a global alliance to transition from coal entirely. Mr. Gordon-Jones explained that the UK is working hard toward a transition from coal.

*“We have just had 100 hours in the UK of zero coal being used in infrastructure, and it’s a big area of policy for the UK the transition from coal, [and]we do not advocate coal in any of our development spend, we usually do not support coal infrastructure projects”<sup>76</sup>.*

The role of MDB’s is to ensure the infrastructure is sustainable, and now renewables are more cost-effective. China is keen that the AIIB is not seen as a vehicle for government policies from how much lending it gave to India for example, it is not a vehicle for the Belt and Road, it is a new Multilateral Development Bank, is led by China but not run by China. That’s why shareholdings come from a range of different countries, including OECD, developed countries.

Concerning the AIIB and the overcapacity issue, it is implicit that the former is not being used as a vehicle to reduce overcapacity in China because it is not going to be lending enough to make a big difference, policy banks such as the China Development Bank, China Exim Bank are already lending much greater volumes. Regarding open tender procurement, in the European Union, there are rules for open tendering, so even the AIIB is following open tender procurement not just for significant infrastructure lending. There are implicit policy banks, China vehicles State-Owned Banks, and the AIIB is the vehicle for open tender procurement. Regarding the Sino-Indian ties, India and China have an interesting relationship, sometimes quite challenging including some land disputes. They both are over a billion people; they have fast-growing economies, and both play highly active roles within their institutions. India is such an essential player in the AIIB, and this demonstrates that China is serious in not willing to politicize the institution, and it genuinely contributes to infrastructure in a way that was impossible

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<sup>76</sup> The author interviewed Mr. Rhys-Gordon-Jones, First Secretary of Financial Policy of the British Embassy in Beijing, for the purpose of this work

before. Moreover, being an inclusive institution, again China is serious about a rule-based system through the AIIB, and the countries should be welcoming.

Anti-corruption rules are really important to the UK which contributes to anti-corruption rules making sure that the AIIB does not contribute to corruption, and is very clean and transparent and having as much transparency and accountability as possible is the only way of freaking out corruption and the AIIB needs to follow high standards otherwise it will have horrible reputation consequences for that.

The AIIB because of this membership, because of its rules and operations and principles and because it is investing in India and in other countries that are not part of the Belt and Road is not made possible to use for the way as mentioned before, i.e., government policies. Open procurement is incredibly important because there is a diverse range of implement. It's hard to see the AIIB be a vehicle for the government's policies, and it does not have enough control to do those more foreign policies and security-based projects. It can be seen as a means of soft power, however, China again is committed in willing to contribute to a serious rule-based international system to demonstrate that there is a strong will to contribute to global goods, such as development in a way which is not politicized, in that way the AIIB will contribute to a positive impression of China to the Asian region. A strong message came from the President at the Belt and Road Forum who listened to the criticism in particular on environmental standards. Pressure from countries like Italy and the UK is having an impact regarding issues such as those just mentioned, and China is listening to that and responding. The AIIB is a vehicle for showing China's commitment to a rule-based international system and multilateralism.

UK had a different opinion about joining the AIIB from Japan and the US. The UK thought that it was better to influence from the inside than influence from the outside. The US took a different approach, they decided not to be part of the AIIB, and they thought disengagement would be a practical approach. Being an active participant in it was the key; nonetheless, the UK has very mature relationships with the US and Japan, two very close relationships, and they contribute to everything all the time. Joining the AIIB was a scenario in which the UK decided to take a different path.

The ADB is a Japanese-led Development Bank, and China saw a problematic avenue to expand its infrastructure in Asia through this Bank. It is headquartered in

Manila, in the Philippines, so it's harder for Chinese to play a creative role. Moreover, China was frustrated for the pace of reform of other MDB's including the World Bank as well, there was an evident frustration on how the system has not adapted to the increasing Chinese economy and a new Multilateral Development Bank was created from scratch in order to reflect the new role. However, China will continue to engage in those other Banks. The AIIB was purely a pragmatic solution to the Chinese new role, and the decision was taken because the other systems would not have been quick enough and at the same time those proper institutions were not able to adapt in time.

The AIIB has the opportunity to improve the global economic governance, and that's why the UK is engaging, however, if high standards of governance were not ensured the UK would not have joined. On this issue, the UK is a passionate advocate for strong economic governance in the future and the only way to advocate strong governance is to be an active participant in it. The AIIB will help achieve the aims of the Belt and Road; obviously they are approaching the same market, but the AIIB's offer is differentiated. It is active in countries that are not in the Belt and Road, it has open sounds procurement, but it is not a vehicle for pure government policies. Since the AIIB is multilateral it cannot be described as a Belt and Road institution.

The Belt and Road can also be described as a way of China to exert global influence, and the UK engages in it in line with UK interests being conscious that there are some risks about the Belt and Road as of many other UK allies that are working with China in order to mitigate them. The Belt and Road is more a China vision of the world, fostering infrastructure and connectivity in the region, so far it has been dominated by Chinese state enterprises and Chinese finance. UK's engagement is to make sure that it is much more internationalized, that's a way in which the UK can increase standards.

Regarding the AIIB as a project connected to the internationalization of the RMB currency we can say that the RMB accelerated a lot in the last years, there is a big push to get the inclusion of the RMB in the IMF SDR basket. China achieved that, but there are a lot of forms to open up and meet the conditions of the SDR. Now it is very tough to get capital out of China and get capital into China. The process is going to be long; it is not going to happen very quickly. There is still no free flow of capital. The AIIB currently lends in dollars, but in the future, it can be lending in RMB. UK's City of London is the

largest center of trade of RMB from the state product, and the UK can play a role in the internationalization of the currency. Furthermore, the UK is deepening its links across the whole world, and it is keen to advocate trade links to the county itself regardless of what happens with the European Union.

### **3.1.3 The case of Italy**

EU Member-States are allowed to join or not on their own according to the EU's institutional structure. Italy for instance, decided to join the AIIB as a founding member, and the decision to ratify the Agreement was directly entitled to the President of the Italian Republic, it was not delegated to EU institutions. Regarding financial duties instead they are up to the Ministry of Economy and Finance<sup>77</sup>. At the time of writing, Italy also joined the BRI in March 2019. Chinese President Xi Jinping visited three other European countries on that occasion, but the response was not unanimous.

Italy joining the Belt and Road Initiative can be compared to the UK joining the AIIB. As a matter of fact, Italy on March 14, 2019 was the first country of the G7 to join the initiative. The country signed a non-binding Memorandum of Understanding. In this document the partnership with the AIIB is emphasized. The involvement of the AIIB in the BRI in Italy has a potential outcome for both countries. Whether the other countries of the G7 will also join the BRI in the short term is still unknown. However, European countries joined the AIIB at different times according to each country's procedures in the process of parliament ratification.

## **3.2 Comparing the AIIB to other MDBs (ADB, NDB, AfDB)**

### **3.2.1 The AIIB and the Asian Development Bank**

In this paragraph, I will compare the AIIB and the ADB from an institutional point of view. These two MDBs are similar because they share a geographic similarity in the region of operation and membership. The US and Japan are the only countries that

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<sup>77</sup> Atti Parlamentari (2016)

decided not to join the AIIB. More than half of members of the ADB joined the AIIB. The former also includes Timor-Leste, Papua Nuova Guinea and the Pacific islands which have not yet joined the latter. The ADB has celebrated 50 years of development partnership in the region with a total of 67 members and 48 regional ones. While the Asian Development Bank was closely shaped on the World Bank, the AIIB better follows recent MDB initiatives. Moreover, they both focus on infrastructure lending; however, the ADB has much more experience since the AIIB had only begun operations in January 2016.

Regarding the areas of finance and membership, the AIIB has an innovative approach, while in terms of voting, it has mainly a conservative approach. According to the structure of the new China-led Bank, it has brought some innovations for governance; however, it is still too early to point out the impact. The Asian Development Bank is similar to the AIIB in particular regarding the purposes and the functions. It was established on the December 19, 1966, and it is a Regional Multilateral Development Bank. According to the Agreement Establishing the Asian Development Bank Article 1 states that the purpose of the Bank is “to foster economic growth and cooperation in the region of Asia and the Far East and to contribute to the acceleration of the process of economic development of the developing countries in the area, collectively and individually”<sup>78</sup>.

Moreover, the Bank should have the following functions:

- i. “to promote investment in the region of public and private capital for development purposes;
- ii. to utilize the resources at its disposal for financing development of the developing member countries in the region, giving priority to those regional, sub-regional as well as national projects and programs which will contribute most effectively to the harmonious economic growth of the region as a whole, and having special regard to the needs of the smaller or less developed member countries in the region;
- iii. to meet requests from members in the region to assist them in the coordination of their development policies and plans with a view to achieve better utilization of their resources,

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<sup>78</sup> Article 1 of the Agreement establishing the Asian Development Bank

making their economies more complementary, and promoting the orderly expansion of their foreign trade, in particular, intra-regional trade;

iv. to provide technical assistance for the preparation, financing, and execution of development projects and programs, including the formulation of specific project proposals;

v. to co-operate, in such manner as the Bank may deem appropriate, within the terms of this Agreement, with the United Nations, its organs and subsidiary bodies including, in particular, the Economic Commission for Asia and the Far East, and with public international organizations and other international institutions, as well as national entities whether public or private, which are concerned with the investment of development funds in the region, and to interest such institutions and entities in new opportunities for investment and assistance; and

vi. to undertake such other activities and provide such other services as may advance its purpose" <sup>79</sup>.

Through the analysis of the Articles, there can be detected many similarities between the two MDB's. However, regarding the membership, the main difference is the absence of both the US and Japan. Moreover, the ADB did not have the same success as the AIIB, the former is mainly an old institution, with not enough resources to address the financial needs of the region.

### **3.2.2 The AIIB and the New Development Bank**

The New Development Bank is a Development Bank which was promoted by BRICS countries i.e., Brazil, Russia, India, China, and South Africa. India advanced it in 2012 during the fourth BRICS summit held in New Delhi; however, it was finally launched one year later, in 2013 during the fifth BRICS summit. The legal basis was set according to the Articles of Agreement. The capital was set at 100 billion USD. The NDB Director is Indian, K.V. Kamath, and the Bank is headquartered in Shanghai. The New Development Bank was institutionalized when the AIIB was announced. Compared to the AIIB, the NDB is more exclusive and dominated by BRICS countries not only in the

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<sup>79</sup> Article 1 of the Agreement establishing the Asian Development Bank

governance but also in its purposes. The two institutions are two different projects, since they have various objects, whereas the AIIB includes Western countries and is based on win-win strategies, the NDB was founded as an alternative to the American ruled Bretton Woods financial institutions. Moreover, the role and weight of China in these two compared institutions is also different, in the NDB each founding member owns the same amount in terms of capital share; in the AIIB China's capital is much higher and paradoxically equal to the NDB's initial capital<sup>80</sup>.

The purposes are different from the ones of the AIIB. The NDB purpose is more restricted, and Article two describes its aim which is "to mobilize resources for infrastructure and sustainable development projects in BRICS and other emerging market economies and developing countries to complement the existing efforts of multilateral and regional financial institutions for global growth and development"<sup>81</sup>.

The founding members of the Bank are only BRICS countries; therefore, western countries did not join the Bank. Instead, the AIIB is a constructive forum that sees the participation of Western countries as founding members which with their contributions provided expertise and experience proving once more the multilateral spirit of the AIIB. Also, concerning the election of the President, the two MDB's are different. The NDB's President is elected from one of the founding members leaving no space for other countries voices to be heard. Therefore, for now, there are no prospects for future improvements in the NDB, which once again is a Development Bank which has not proposed new ingredients to reform the international financial architecture.

### **3.2.3 The African Development Bank and the AIIB**

The AfDB is regionally focused, such as the ADB, and it is founded to contribute to the social progress and economic development of the African region, contributing to poverty reduction. It was founded in 1964 and like the WB has three leading agencies: the AfDB, the African Development Fund and the Nigeria Trust Fund<sup>82</sup>.

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<sup>80</sup> Humphrey (2015)

<sup>81</sup> Article 2 of the Agreement on the New Development Bank

<sup>82</sup> AfDB website

The African Development Bank's Agreement was adopted in 1963. The Agreement entered into force in 1964 and the Bank started its operations in 1966. The Bank aims to foster development in its regional members individually or as a whole<sup>83</sup>.

China became a partner of the African Development Bank and the African Development Fund (ADF) a long time ago, in 1985. In order to promote Africa's development and sustainable growth, the two countries are cooperating in trade, investment, and infrastructural development. The AfDB has signed Memoranda of Understanding with the Export-Import Bank of China, China Development Bank the Agricultural Bank of China, and the AIIB. Moreover, the two MDBs are following the highest standards regarding level of transparency and openness, and both have the same vision and complement each other. The AIIB is not currently financing projects outside Asia. In the future the AIIB will cooperate with the AfDB in Africa if and only if those projects will benefit also the Asian region. At the moment China Development Bank and China Exim Bank are financing mostly of the projects in Africa.

### **3.3 Cooperation with other MDBs**

As a member of the group of development banks, the AIIB has signed several Memorandums on joint cooperation and co-financing with: the African Development Bank, the African Development Fund, the Asian Development Bank, the Eurasian Development Bank, the European Investment Bank, the Inter-American Development Bank and Inter-American Investment Cooperation, the Islamic Development Bank Group (IsDB Group), the New Development Bank and the World Bank Group. There is also an ongoing partnership with private financial institutions in non-governmental sectors. It was also argued that the AIIB is not competing with established MDBs such as the World Bank and the ADB since they both focus on poverty alleviation. For co-financed projects, the AIIB is currently complementing the existing financial institutions. Moreover, according to Chinese analysts, Asia was lacking in platforms to mobilize financial resources. The World Bank and the Asian Development Bank are just two of many IOs in which countries collaborate in order to provide aids to developing countries. During an

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<sup>83</sup>Agreement Establishing the African Development Bank. Khartoum 4 August 1963



interview with the editor of the Financial Times, on March 31, 2015, Premier Li Keqiang stated that the AIIB was not meant to reinvent the wheel, and that China had no intention of challenging the current international financial system, but rather that it wanted to contribute to its healthy development<sup>84</sup>. Moreover, the AIIB borrows the experience of the World Bank and ADB since many former World Bank and ADB employees' have been advising the Chinese government over the AIIB<sup>85</sup>. The President of the AIIB, Jin Liqun, worked both at the World Bank and the Asian Development Bank before taking up the position at the AIIB. As a consequence, he brought his experience and knowledge to design from scratch the AIIB, which is mirroring the existing multilateral banks. The World Bank and the Asian Infrastructure Investment Bank signed a Memorandum of Understanding in Washington D.C. on April 23 to strengthen cooperation on multiple areas between the two multilateral development institutions<sup>86</sup>.

The President of the AIIB, Jin Liqun, stated that "Signing this memorandum of understanding fits into our vision of a new kind of internationalism, we place a high value on our partnerships because by working together, we greatly increase our potential for positive outcomes in Asia"<sup>87</sup>. Furthermore, the President of the World Bank, Jim Yong Kim, which became World Bank president in April 2012, stated that "A collaboration between development institutions is essential to make the best use of scarce resources, a crow in the private sector, and meet the rising aspirations of the people we serve"<sup>88</sup>. With the signing of the memorandum of understanding, the two multilateral development banks (MDBs) agreed to cooperate on projects to be co-financed in 2017 and 2018. In 2016 the AIIB co-financed the first project, a new highway in Pakistan Punjab province, with the Asian Development Bank in Pakistan<sup>89</sup>. Joint projects with the ADB have been approved. For example, in Pakistan, the project of China-Pakistan Economic Corridor (CPEC) that links China's Xinjiang to Pakistan's deep-water port Gwadar will reduce dependence on the Malacca Strait.

Moreover, in the Punjab province, another project will be carried out. The construction of the National Motorway M-4 which will connect various parts of Pakistan

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<sup>84</sup> China Daily (2015a)

<sup>85</sup> Wan (2016)

<sup>86</sup> China Daily (2017)

<sup>87</sup> World Bank (2017)

<sup>88</sup> Ibidem

<sup>89</sup> Reuters (2016)

and will facilitate trade in the region from Central Asia to the seaports of Gwadar and Karachi. According to public documents, the project will be implemented in the period from June 2016 to June 2020. Furthermore, since the signing of the Co-Financing Framework Agreement for investment projects in 2016, the AIIB and the World Bank have co-financed several projects that support the energy sector and industry in Pakistan, in Azerbaijan, and regional infrastructure development in Indonesia<sup>90</sup>.

Besides, the International Finance Corporation, member of the World Bank, and the AIIB have co-invested in a power sector project in Myanmar and are figuring out other future projects. As it was mentioned before, one of the projects co-financed with the World Bank will improve the hydropower and energy sectors in the Republic of Pakistan. The AIIB has lately also agreed to enhance collaboration with another MDB, the Eurasian Development Bank, in common areas of interest across Eurasia. On December 3, 2018, the MDBs committed on working together in six central key areas to meet the goals of the Paris Agreement, underlining their willingness to commit in order to tackle climate change. As the Asian Development Bank reports “the joint declaration was issued when the 24th Session of the Conference of the Parties to the United Nations Framework Convention on Climate Change (COP24) started, in Katowice, Poland”<sup>91</sup>. The plan is to align the operations against mitigation and climate-resilience goals to tackle climate change in developing and emerging economies.

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<sup>90</sup> World Bank (2017)

<sup>91</sup> ADB (2018)

## **Chapter 4 China and the EU: Global economic governance in the framework of the AIIB**

This chapter analyses the case of the AIIB as a tool to enhance global economic governance between China and the EU. Moreover, since the establishment of diplomatic ties between the two countries, there has been an active collaboration on multiple issues.

### **4.1 How has the EU responded to the AIIB?**

Since the establishment of diplomatic relations 40 years ago, the China-EU relationship has made progress through joint efforts. Their relationship will be vital and one of the most critical bilateral global relationships of this century. Moreover, China will establish a comprehensive strategic partnership for mutual benefit, since the two sides have been promoting together world peace and joint development.

Initially, the EU looked at the AIIB China-led initiative with suspicion, especially regarding the impact of it in the long term. The initial suspicion regarded to which extent the Bank would have been with Chinese characteristics, à la Chinoise and follow Beijing's agenda. Although China politicians initiated the creation of the AIIB, that did not mean that they have full control over how it is managed, especially considering how the international community responded. Many European countries participated in the AIIB because they foresaw that it was the only way to influence its direction and that the Bank was a possible solution to much-needed infrastructure in poor countries in Asia. Already many MDBs such as the World Bank, ADB, and EBRD have a strong presence in Asia, however, infrastructure needs were not fully met to the high demand in the region.

According to a report issued by the ADB<sup>92</sup>, it has been estimated that by 2030, Asia's infrastructure needs will rise to \$22.6 trillion needed to cover growth rates.

In order to better comprehend the difficulties of the engagement of both the EU and China, the particular institutional design will be outlined. Different from the Westphalian international system - or called the world community - which characterizes Western countries, the Chinese world order is instead hierarchical, morality-based, and Sinocentric with China at the center of it. Regarding the institutional design of the two polities such as China and Europe, often these differences can create obstacles in coordinating together. Recalling Sergio Fabbrini's lectures, according to him the EU is classified as a "compound democracy"<sup>93</sup>, since it is based on a compound structure of functionally independent and politically interdependent legislative, executive, and judiciary bodies. The EU is a hybrid model between a federation of states and a federal structure, in which the Parliament is in charge of the legislative power, the European Court of Justice of the judiciary and the Council and the Commission are a dual executive; so, all these institutions act in synergy within a governmental and compound law-making based on a separation of powers and functions. Market and financial policies are managed by the council, but each member state retains its own fiscal system and wealth. This design paved its way to asymmetry and inefficiencies in the absorption of economic shocks. Example lies in the economic 2007-2008 recession that crippled the world economy, especially European strongholds like Iceland and Germany.

In contrast to the EU structure, China embodies the definition of "one-party state". The four powers – legislative, executive, judiciary, and military – are divided, but the government relies heavily on the Chinese Communist Party (CCP). It is a centralized structure which follows the ancient Confucian tradition. When it comes to diplomacy and foreign policy, China's practices rely on "Track II" diplomacy with the interaction of think tanks, NGO's, academia and Track I diplomatic environments and policymakers<sup>94</sup>. Because China is more united on these fronts China is able to have more collaborative outcomes than the EU that appears to benefit the country as a whole. Regarding the landscape of financial institutions within the realm of development projects, there is a

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<sup>92</sup> ADB (2017)

<sup>93</sup> Fabbrini (2010)

<sup>94</sup> Tan (2007)

plurality of them, from the Export-Import Bank of China to the recently established Silk Road Fund and the Asian Infrastructure Investment Bank. Concerning the AIIB, many EU member countries, but not all, engaged in the initiative in order to be able to influence the new MDB from the inside and make sure that it would follow multilateralism and make sure it wasn't completely Sinocentric.

As discussed in Chapter 3, during the negotiations of the AIIB, 14 EU member states - Austria, Denmark, Finland, France, Germany, Hungary, Italy, Luxembourg, the Netherlands, Poland, Portugal, Spain, Sweden and the UK - took part to the initiative and many were also founding members. The transatlantic alliance did not have a common policy to whether to join the AIIB or not. This can be linked also to the lack of common foreign policy in the EU. On March 12, 2015, the UK became the first major industrialized country to join the Bank. After that a snowballing effect took place. On March 17 Germany, France, and Italy decided to join. They saw this as an opportunity to help influence Asian countries to build something new based on sound principles showing that the AIIB was complementing the world architecture. Since so many European countries were interested in joining the AIIB, the European Union (EU) should further engage with China in order to promote interests, common interests, in the broad context of multilateral institutions. China's global governance policies currently have and will have an impact on the EU. It is vital that European constituencies work together in order to push and achieve higher standards of accountability and transparency. However, the approaches of China and the EU to reform global governance have some commonalities and some differences which will be explained in the following paragraphs.

China's rise in the context of global governance is having a substantial impact both on regional and world architectures. This shift in power distribution from West to East will inevitably have an effect. Many concerns arose regarding China's willingness to establish an international order which is new and not following the existing system laid out after WWII. The EU realized it should engage more and welcome change, but at the same time, it should mitigate risk and be cautious of different ideologies.

The AIIB is not the only economic initiative that was launched in 2014; two other financial institutions, the New Development Bank of BRICS countries and the Silk Road Fund were also established. The Chinese landscape is complicated when it comes to financial institutions playing a role in developing projects; there is a plurality of financial

institutions ranging from China Development Bank (CDB) and China Exim Bank to the newly established Silk Road Fund and the Asian Infrastructure Investment Bank.

These initiatives all took into consideration that China is a player who will shape the financial engine to a new development model that no one has ever engaged with before. Since they are coming in hot and heavy with a lot of capital, economic stability, and human capital, China's prominence in international economic relations has been perceived as threatening to the current world order. Where concerns may be valid proves to be yet determined. Regarding the AIIB, the European shareholders should bring the expertise, resources, and staff in order to have closer monitoring on the AIIB's implementation of projects. As long as China is willing to take into consideration the western rule-based system and listen to advisement on best practices, European countries should be welcoming to their points of view. Of course, higher standards should be pursued regarding the environment, human rights, and governance. There is an evident Chinese dissatisfaction with the existing International Financial Institutions, and China has the ability to influence the world order like never before. However, China is still a developing country as the WTO and the UN define, but not as developing as in the past. This can be illustrated by their slowing growth rate over the last 3 years. Now the "rejuvenation" expressed by the Fifth generation of leaders has the priority of many interests at stake such as to guarantee political and economic benefits<sup>95</sup>. The AIIB, among the other initiatives of China, will be the protagonist of this shift from a Western-led governance' (*西方治理*) to a more inclusive East-West co-governance' (*东西方共同治理*). However, China's rise will not lead the country to a global hegemonic power, at least according to the Chinese perspective. China has a different view on how the global economic governance (GEG) should be in the future. It's still to be determined what impact the new Chinese-led financial institution will have with regional initiatives launched by the EU, for example the Juncker Plan.

As mentioned earlier, the EU has not always been unified in their policies regarding engagement with China, as member states joined the AIIB independently. However, there are some examples where they coordinated effectively to enhance their own interests. The Joint Statement of the 14<sup>th</sup> Meeting of the EU-China Roundtable which

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<sup>95</sup> Menegazzi (2017)

was held in Brussels between 18 and 19 of May 2016 stressed the pivotal importance of the EU's strategy towards the AIIB and the agreed upon the entrance of China into the European Fund for Strategic Investments (EFSI). Moreover, the round table between the European Economic Social Committee and the China Economic and Social Council recognized the compatibility of objectives of the Europe 2020 strategy and China's 13<sup>th</sup> Five Year Plan<sup>96</sup>. The Europe 2020 Strategy was advocated in 2010, and it aims to promote long-term policies in order to prioritize smart, sustainable, and inclusive growth. A strategy which will bring stronger governance as a result. Moreover, according to the European Commission, when member countries conduct bilateral relations with China an enhanced cooperation with the Commission, the EEAS should be pursued in order to ensure that the possible outcomes will be in line with EU law, rules, and practices, and that the result will be beneficial to the EU<sup>97</sup>. Despite these advancements in unification, there are still gaps that need to be addressed. During an interview with Giovanni Garcea, Head of the Economic and Financial Section of the Delegation to the European Union to China, it emerged that there is still a lack of a unified European approach to the AIIB and China's initiatives. The solution should be a more cooperative and coordinated approach with a cohesive EU strategy. With no doubt, China prefers to interact bilaterally with the Member States, and as long as European Countries don't have a common EU position vis-à-vis China and the BRI, the situation won't change.

Moreover, regarding the AIIB, it still has to be seen how it will address the debt sustainability issue and environmental issues respecting the EU practices and laws. China sees Western Europe as a strategic area that has assets and multiple development networks, instead, Central Eastern Europe (CEE) is seen as a platform and as an access to Europe for China to deliver its goods<sup>98</sup>. CEE countries include both EU and non-EU members and are addressed by a Chinese strategy to boost infrastructure projects through institutional banks such as China Export-Import Bank or China Development Bank. The fact that many Western countries joined the AIIB enhanced the credibility of the new Beijing based Bank. The United States, instead, as mentioned already in Chapter 3, did

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<sup>96</sup> EESC (2016)

<sup>97</sup> European Commission (2016)

<sup>98</sup> Zeneli (2016)

not join, also because the hegemon shifted its attention to Asia at the same time through the Trans-Pacific Partnership (TPP). The United States also engaged with the EU through the Transatlantic Trade and Investment Partnership (TTIP). It can be argued that the momentum in which China decided to play a more proactive role in international affairs, acquiring more legitimacy and international recognition, will be at the expenses of the United States. During a talk with my Chinese professor and supervisor of the Chinese thesis, Wei Ling, it emerged the fact that the creation of the AIIB is a means created by China to not engage directly with the US in the Asia Pacific region.

The EU-China Summit, which took place in Brussels, April 9, 2019, strengthened the ties between the two countries and reaffirmed the strength of their Comprehensive Strategic Partnership. The two sides committed to work together and advocated the UN Charter, international law, and the three pillars of the UN: peace, security development, and human rights<sup>99</sup>. In addition, the two countries emphasized the need to explore areas for enhanced cooperation and they both committed to the implementation of the 2030 Agenda on Sustainable Development. Regarding global challenges and governance, the EU and China both support the WTO rule-based trading system and launched an initiative to comply with its rules. Furthermore, strong support to the G20 forum in international economic and financial cooperation was reaffirmed. Concerning the environment, the two countries both advocate for a more environmentally sustainable economy and are working together for the accomplishment of the UN's Sustainable Development Goals.

Summarized, the EU responded quite well to the establishment of the AIIB and China's attempt to be more involved in world politics. Since several countries have joined, they are trying to positively affect the AIIB policies and provide expertise, influencing development in Asia. However, more cohesive collaboration by the EU member states is needed in order for this Bank to truly benefit the EU. Therefore, the creation of the AIIB is unconsciously forcing the EU to think more as a unified entity than as separate member states which is a good thing for Europe. China is complementing the world order quite nicely.

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<sup>99</sup> EU-China Summit Joint Statement, Brussels, 9 April 2019, European Union and China.



## **4.2 Cooperation with EU MDBs**

MDBs should not promote unhealthy competition and cannot serve as building blocks; on the contrary through development solutions, they should spur positive spillovers and vertical and horizontal collaborations between MDBs should be encouraged.

Besides, the AIIB can borrow experience and learn from their European counterparts regarding coordination at the institutional level, cooperation at the portfolio level, and co-optation at the project level<sup>100</sup>. In this regard, the AIIB can draw important lessons from its European counterparts, Europe has two leading regional MDBs: the European Investment Bank (EIB) based in Luxembourg, and the European Bank for Reconstruction and Development (EBRD) headquartered in London. According to the research question of the thesis, it is relevant to give an outlook of the EBRD and the EIB and their ongoing cooperation with the AIIB. In the realm of infrastructure financing, the EU and China are present with multilateral cooperation, and the EIB is the financial tool through which cooperation can be enhanced.

### **4.2.1 The European Bank for Reconstruction and Development and the AIIB**

The European Bank for Reconstruction and Development is an international financial institution that was founded in the 90s. It differentiates itself from traditional MDBs since from the Article 1 of the Agreement Establishing the European Bank for Reconstruction and Development. It aims to foster a transition to market-oriented economy<sup>101</sup>. Being established in 1991 after the Cold War when the Soviet Union collapsed, it was aimed for financing European countries which were under the influence sphere of the Eastern Block.

Through the years the focus of the EBRD expanded, and it also started operating in Central Asia and Southern and Eastern Mediterranean regions. Notwithstanding the name of the Bank, the main shareholder is the US. The principal shareholders are 67 and

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<sup>100</sup> Xianbai (2017)

<sup>101</sup> Agreement Establishing the European Bank for Reconstruction and Development. Article 1

come from the five continents with the EBRD and the EIB. China and India are the new countries that adhered to the Bank. The EBRD has a robust political implication; one of the main objectives of its mandate is to apply the principles of multi-party democracy and pluralism, which differentiates the EBRD to the AIIB. As a matter of fact, the AIIB firmly embeds the no strings attached policy, whereas the launch of the EBRD was linked to the purpose of influencing the countries it financed from a political and economic perspective. While the limits of the ADB and the WBG consist in a large number of shares held by Japan, the US and western countries, the principal limit of the EBRD is the nature of its operations i.e., political nature.

The two Banks have signed a Memorandum of Understanding in 2016 and have co-financed many projects in sectors such as infrastructure and gas pipeline. The Chief of the EBRD Chakrabarti underlined the potential outcome of the MOU since the EBRD was the last development bank created, the AIIB can learn from its experience from the beginning. Moreover, the EBRD is the leading investor in Central Asia so far and can provide the China-backed Asian Infrastructure Investment Bank with the necessary expertise and performance requirements regarding transparency in public procurement and following high environmental and social standards.

## **4.2.2 The European Investment Bank and the AIIB**

The European Investment Bank, with the European Investment Fund forms the European Investment Group. It was established in 1958 when the Treaty of Rome came into force. It works with more than 150 non-EU states. In 2016 the EIB signed a new partnership with the AIIB intending to increase cooperation in countries where they are both present. Moreover, an exchange in expertise in technical and financial domains occurred. More importantly, the EIB can help the AIIB in tackling climate change issues, since the EIB is the world's promoter and lender of green bonds.

Luxembourg, the first European country that applied for membership in 2013 and joined the AIIB as a founding member in 2015, will be hosting the first Asian Infrastructure Investment Bank's meeting outside Asia which will be held on July 12-13, 2019, in Luxembourg City. The theme will focus on "Cooperation and Connectivity" regarding the realization of better connectivity within countries and regions, including

Europe and Asia. A Memorandum of Understanding was signed by the Minister of Finance of Luxembourg, Pierre Gramegna and Sir Danny Alexander, Vice President and Corporate Secretary of the AIIB. The words of the Minister of Finance of Luxembourg regarding the 2019 Annual Meeting are positive since it will be an opportunity for enhancing cooperation and collaboration for developing better infrastructure to connect Asia and Europe. Moreover, Luxembourg is the leading EU financial center and host of major European institutions, including the European Investment Bank and the European Stability Mechanism, so it will be an opportunity to gather members, prospective members, partner institutions, business leaders, and civil society for deepening the dialogue also concerning the tightening of ties between the AIIB and European partners.

### **4.3 China's approach to economic diplomacy**

In order to understand how China can contribute to global economic governance it is useful to understand when China underlined the willingness to use the term global economic diplomacy. Only in the 12<sup>th</sup> Five-year Plan Xi Jinping highlighted the need for China to engage more in the GEG and the AIIB can be considered as a tool for this objective. Three key Chinese terms analyze the combining of economics and foreign policy: economic diplomacy (*jingji waijiao*), trading power (*maoyi qiangguo*), and financial security (*jingji anquan*)<sup>102</sup>. The three concepts are linked together because they involve the financial dimension, economic diplomacy, and reliable trading power. Recent major commercial initiatives have underlined China's willingness to play a more assertive role, and this is also linked to a dramatic change in Beijing's policy. Already the first generations of leaders of the People's Republic of China, took into consideration economics when practicing diplomacy. However, the concept of economic diplomacy appeared only during the reform and opening up period when Deng Xiaoping promoted a turn toward "foreign-oriented economic policy" (*duiwai jingji zhengce*). China's reforms followed a policy which according to Deng's words was aimed to "bring in foreign knowledge, technology, and investments to help China develop" and emphasized the importance of bringing the expertise from the West<sup>103</sup>. In the 1980s, Chinese leaders were focused on stabilizing the position of China internationally and pursuing

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<sup>102</sup> Heath (2016)

<sup>103</sup> Liu (2003)

modernization of the economy. Diplomacy was serving the economic development of the country. China experienced a change in the use of economic diplomacy when Beijing applied for the accession to the World Trade Organization in 2001. China's voice was increased in the international economic order, and it expanded with the Group of Twenty (G-20), Asian Development Bank, Association of Southeast Asian Nations (ASEAN) plus three<sup>104</sup>, Asia-Europe Meeting and other organizations.

#### **4.4 China's view of global economic governance**

China's rise has brought changes to global governance, in particular, in the financial realm. In purchasing power parity terms, it has surpassed the US in the last years, and as a consequence, the rise of China as a global economic power has implications in the global economic governance. Since 2010 the Chinese economy has become the second largest in the world. The AIIB which many consider as an alternative to the World Bank has gained a lot of consensus from the American allies, and this can be seen as a failure of American diplomacy. Moreover, China's recent economic policies have increased tensions with the US because they are challenging the status quo of the richest and arguably most powerful nation in the world. President Xi Jinping strongly defended globalization and its implications in Davos in 2017<sup>105</sup>. Especially after the 2008 global financial crisis, China and Chinese scholars began to discourse on global economic governance. With no doubt, a power shift is occurring, and China is playing a proactive role in the international arena. The primary key institutions of global economic governance, the Bretton Woods Institutions and the World Trade Organization (WTO) are often put at the center of the debate. China never had a long history of collective discussion of global economic governance since the country joined IOs only recently and after significant reforms. Moreover, being China, a global commercial player it should contribute more to the transformation of GEG.

However, the concept of "global economic governance" was a taboo in China until the early 1990s, and the concept was adopted only after the 2008 financial crisis. The crisis significantly affected China's identity and the evaluation of international political landscapes. We have to keep in mind that in the past decades, China has been following

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<sup>104</sup> the ten members of ASEAN plus the PRC, Japan, and South Korea

<sup>105</sup> CGNT (2017)

Deng Xiaoping's principle, "keeping a low profile" that underlined the importance of domestic affairs rather than international ones. As a matter of fact, China concentrated on internal reforms and the development of the country. Moreover, being a developing country, it has never considered providing global leadership or participating in global governance. As a consequence, China has only recently adopted its theory of global economic governance which is not so distant from the one of the West, however, it has been shaped differently according to the necessities of China. China has to find a role in the global governance architecture. Chinese foreign policy has changed through the years according to the different leaders' aspirations for the country and according to the needs for the development of the country. China's strategy has followed for many years Deng Xiaoping's vision of "keeping a low profile", which characterized decades of development and avoidance of primary international responsibilities. Nowadays, the concentration on domestic development is always put forward by the present leader however Xi Jinping exerted a move from a global system taker to a system shaper<sup>106</sup>.

Today's perspective is different because the global landscapes and China's role in the world order have changed. The size of the Chinese economy cannot follow the principle of keeping a low profile. As a matter of fact, from Deng Xiaoping's keeping a low profile scenario, Xi Jinping opened a new era with a foreign policy based on 奋发有为 (*fenfa you wei*), or striving for achievements. The latter implies that China should promote reforms within the current system, and at the same time, it should adopt and participate in this mechanism. Another possible scenario is for China to start to establish a new rule system or global economic order in which the country dominates. The role of the state in China is different from the role of the state in Western countries. It plays an overwhelming role in socio-economic affairs, and the country is characterized by a one-party system that considers NGOs and civil society as a threat. As a consequence, Western theories that take into consideration governance without government are not possible to be applied to China's case. The West has generated the current global economic theory. The big question of the twenty-first century is how the future world order will be shaped after China's major initiatives.

Besides, the so-called "Thucydides' Trap" developed by the scholar Graham Allison should be avoided. According to the scholars' theory<sup>107</sup>, there could be a

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<sup>106</sup> Jinghan (2019)

<sup>107</sup> Allison (2017)

potential conflict leading to a confrontation in US-China relations. The situation in which there will be a Chinese predominance in global governance, this will also undermine American hegemony. According to Ikenberry<sup>108</sup>, the rise of China can pose two potential evolutionary scenarios: either China would replace the rules and practices of the West becoming a challenger to the status quo institutions, or more likely China will comply with the Western liberal order, benefit from it and be in accord with a smooth power transition, and this is what this thesis tried to demonstrate. The AIIB can in some way jeopardize the rules of the game in Asia, as Asia is in this moment at the heart of China-US rivalry. However, as argued in Chapter 2, at this moment, the AIIB is following the rules, complies with status quo institutions and cooperates with them.

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<sup>108</sup> Ikenberry (2008b)

## Conclusions

China is playing a major role in shaping global governance. New diplomatic initiatives have contributed to China's proactive role. The Chinese Government is building an international institution at a critical historical juncture. The AIIB is an international organization that garnered much attention being developed by a rising power vis-à-vis status quo powers. The China-led Bank is bringing a change in the development game within an evolving international order. The foreign policy goals are being consolidated by the AIIB's south-south projects. The concepts of China Dream and One Belt, One Road are intertwined and play a huge role in Beijing's assertive foreign policy and search for legitimacy and reputation. The AIIB is complementing these. The institution comes from a nondemocratic country that differentiate itself from the United States and Western Europe in the conception of political economy following a state capitalist version of it. The launch of the AIIB is seen as a great innovation for the global order. It is the first Multilateral Financial Institution created outside the Bretton Woods system to have good success from the beginning. Despite strong opposition from the US, many allied countries have joined the Bank, and some have been founding members. The AIIB had a great response not only from developing countries but also from developed ones which followed the UK's decision.

The aim of this work was to analyze the factors that see the AIIB as a complementing ingredient to the existing international financial order. In order to conduct deep research on the topic, I followed the neo-liberal institutionalism theory. The AIIB is a compromise between innovation and well-established principles. The AIIB as a financial institution is institutionalized on multilateralism not only in the constitutional charter but also in the high standards of the Bank. Moreover, it pursues inclusiveness and a consensus approach in the decision-making process. Multilateralism was pursued from the beginning.

It was useful to provide the context in which the AIIB was launched. The current Chinese foreign policy has played an important role in understanding the governance of

China. The new concepts developed by the Fifth Generation of Leaders are grandiose and they are also present in the new MDB. This thesis argues that the AIIB project resembles the international norms that discipline and guide the existing Multilateral Development Banks. The Bank has delivered higher efficient projects so far, improving the traditional MDBs. Today's international institutions are not responding efficiently to current challenges. The global system is still linked to the past and fails to satisfy the needs of the current one. In particular, developing countries seek an increase in their influence and seek more recognition in the international arena. However, year by year, developing countries are holding more and more shares of the total global economy.

The distribution of power is unbalanced in institutions such as the ADB or the WB. Moreover, higher levels of bureaucracy and high management costs characterize the pre-existing organizations and innovation in this aspect has been brought by the AIIB, for example with the non-resident Board of Directors. From a political perspective unlike the aforementioned institutions, the AIIB differentiates itself in the non-politicization of its operations. By trying to follow the principles of not interfering and mutual respect underlined also in the Beijing consensus the AIIB seems to bring innovation. From the first few years of activity, most of the projects have been co-financed with other MDBs, and this feature underlines the design of the Bank, which is to complement the existing financial order. The AIIB as an intergovernmental financial institution mostly aligns with international practices, and compared to the ADB, according to the research conducted so far, the former is more efficient and economically sustainable than the latter. The AIIB was a fascinating case to analyze and if it will continue to be a success every country that joined this MDB will benefit from that through spill-over effects.

Furthermore, the AIIB started successfully. Its recognition by multilateral development banks and the UN, as well as top marks from leading rating agencies and the rapid expansion of its membership, demonstrates the bank's successful integration into the realm of the international financial architecture. The AIIB built its business model in the first years of activity, in particular in the context of co-financing. Concerning regulations and procurement, the AIIB aligns with the rules of transparency and public procurement. The EU will continue to accompany the AIIB in this regard carefully and constructively as part of its membership in the bank. The work of the AIIB is in accordance with internationally accepted practice. The AIIB has to commit more to the involvement of non-governmental organizations which can help in the development of strategies and policies through the Bank.



This scenario is less likely to happen since as discussed in this work, the AIIB conforms to the rule-based system and practices and is the product of a narrative based on win-win cooperation and mutual benefit.

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# Summary

## Introduction

This thesis aims to discover and analyze the multilateral features of the Asian Infrastructure Investment Bank (AIIB). The AIIB is a new multilateral development bank that aims to complement development efforts in Asia improving social and economic conditions in the region. The Bank is pretty young, a startup designed from scratch and firstly announced by President Xi Jinping as a tool to complement the OBOR initiative in 2013. My hypothesis is that China is not challenging but rather modifying the existing multilateral international institutions. My research question is whether the AIIB is challenging the existing multilateral financial institutions or not. In order to deliver a comprehensive and exhaustive answer to the research question my thesis is divided in four chapters that analyze different factors that see the AIIB complementing the International Financial Institutions and global financial governance. To conduct this research different materials have been analyzed. The Articles of Agreement of the AIIB were consulted in detail in order to develop an exhaustive analysis of the Bank's purpose, shares, and voting distribution not only in its governance but also in its structure.

Moreover, reports and scholar's papers were utilized to learn both the financial implication and the political one. Official documents, such as the Memorandum of Understanding, also helped deliver a qualitative research of multilateral development banks' main functions. Interviews with specialists of the Bank, Professors of China Foreign Affairs University and further discussions coming from international media and scholars' opinions were valuable sources during the research to strengthen the thesis' conclusions. An overview of both Chinese and European perspectives is the main pillar of this work.

### **Chapter one: Theoretical framework**

According to the research question several theories can be used to investigate the research question and strengthen the conclusions of the hypothesis. So, the hypothesis is analyzed through the neo-liberal institutionalists' theories.

Neo-liberal institutionalism has proven to be the accurate theory since institutions are perceived as tools to bring win-win cooperation and as means to enhance cooperation and improve information asymmetries. Notwithstanding neo-liberal institutionalism also contested multilateralism was analyzed. Contested multilateralism is used in order to prove that the AIIB as it currently stands is not fulfilling the criteria that identify a situation of contested multilateralism. AIIB follows traditional practices of the status quo institutions and the activities of the AIIB do not shift focus away from institutions like the World Bank. Instead, they complement the development efforts in Asia.

The AIIB is, therefore, the result between Western and Chinese principles of cooperation and development. Even the Bank's President-designate Jin Liqun stressed the principles mentioned above in several occasions. During the whole process of drafting of the Articles of Agreement shareholders have been working collegially to formulate the underlying principles of the bank such as transparency, openness, accountability, and independence. Besides, the guideline of the operations will have a strong policy and governance framework. Moreover, the AIIB will bring innovation in infrastructure financing suitable for Asia's infrastructure needs. The AIIB's slogan and *modus operandi* are "lean, clean, and green," and accordingly these words are specifically the three defining keywords of the Bank; lean, with a highly skilled staff; clean, the ethical *modus operandi* with high standards of anti-corruption; and green, the pillar of this institution which takes care of the environment and respects it. Moreover, multilateralism fosters predictability, transparency, and sustainability, generating "diffuse reciprocity," which is expected to benefit the AIIB membership. In the law of the AIIB, multilateralism is fulfilled in the decision-making process. Consensus-seeking has always been present from the beginning of the establishment of the Bank; in particular, from the signing of the Memorandum of Understanding in 2014 to the official establishment of the AIIB on 25 December 2015. All matters from the initial phase to the formal establishment of the new multilateral institution have been decided by consensus. The consensus approach is also present among the three existing institutions of global economic governance – the IMF, the World Bank, and the WTO.

The mission of the AIIB is to reflect the views, voices, and values of all its shareholders as underlined several times by the President of the Bank, Jin Liqun. However, China has a *de facto* veto power on issues such as the decisions on the size of the Board of Directors, any amendment of the AOA and the election of the President, all of which require a Super Majority vote. The number of veto players in a system has an

impact on its capacity of making decisions and on its stability. In opposition to the US' power in the IMF AOA, there is no similar situation in the AIIB symbolizing China' s transparency in not seeking veto power in the Bank.

Another key element that explains the result of the merging between Chinese and Western principles of cooperation can be detected in the decision of many OECD countries to join the AIIB. The OECD is an intergovernmental forum that allows for collaboration among members of governments on economic, social, and environmental topics. From the beginning, they contributed and cooperated providing OECD principles regarding rules and procedures that were discussed during AIIB's preliminary negotiations. The cooperation between developing and developed countries and the participation of all the shareholders to contribute to the creation of something new based on principles and a good governance structure was the major success of the Bank.

## **Chapter two: Why the World needs the AIIB?**

MDBs seek to reform. The system of the Washington Consensus pushed for the diffusion of neoliberal ideas and policies which became spread globally only in the 90s. Those multilateral rules were formulated inside the EU, the OECD, and the WTO. However, the aim of those rules was not to revolutionize the nature of the policies of supranational economic integration, but instead to standardize them so that no country was excluded from their potential benefits. Beyond the Washington Consensus, we find the European and Beijing Consensus. The European Consensus focuses on a package of measures aimed at primarily favoring development policies in EU's partner countries, and they are centered on three main sectors. These sectors include poverty reduction, development based on European democratic values, and accountability of developing countries for their future. The Beijing Consensus has been advanced as a sovereigntist alternative to the Western recipe that conceives in a non-negotiable way free market with democracy and human rights. On the contrary, for the Beijing Consensus, economic development has to be kept separated from the political sphere. The focus is a commitment to innovation and constant development, GDP as the only parameter to take into consideration for measuring progress and the pursuit of self- determination in terms of public policies.

The diffusion of this new setting, especially in the framework of the policies of the AIIB is the result of the decline of the Western powers. The doctrine of Beijing is emphasizing the development of local enterprises with the aim of self-development, providing aid without political strings attached and pursuing common development based on equality and mutual benefits and finally to keep pace with reforms and innovation. The One Belt One Road Initiative supports the spread of the Beijing Consensus. Opposite to the current success of the Beijing Consensus, the reasons for the weakening of the Washington Consensus can be grouped in two essential dynamics. Firstly, the frequency of crises the South has experienced shows the weakness of the project of financial liberalization, and secondly the rising of social inequality due to the effects of the neoliberal reforms in numerous contexts. Both the World Bank and the International Monetary Fund were established during the negotiations at Bretton Woods in New Hampshire in 1944.

The World Bank was created following the American plan, and contrary to the United Nations General Assembly, both the members of the IMF and the WB did not have equal voting power. The WB had 38 members in 1946, now it is known as the World Bank Group and has 188 members in its International Bank for Reconstruction and Development (IBRD) and 172 members in its International Development Association (IDA). Many critics have been made to the Bank, in particular for its structural adjustment loans that worsened poverty in indebted developing countries. Japan successfully created the ADB, which is a hybrid of the World Bank and the Japanese institutions. The Japanese while building the ADB followed the World Bank experience. The China-led AIIB will be faster and flexible than the existing financial institutions, which will likely be pushed to reform. The AIIB is a functional equivalent of the World Bank and the ADB; however, it is pushing for a no more western-led international structure. The World Bank has implemented reforms regarding the internal governance i.e., “voice reforms.” Despite the reform in the share of votes held by developing countries, the weight of developing countries’ voting shares has not increased substantially. Compared to the United States, Japan, and European Union members, the influence of rising powers is not relevant. Taking as an example the case of China, since the 1970s its influence has increased within IOs. The international development finance architecture is no more centralized, but it has decentralized through structural shifts, and a plethora of multilateral development banks has come up. Through the nascent AIIB, the Asian institutional landscape is on the way of transformation.

Asia needs more infrastructure and international financing and the rapid growth and growing interdependence explain the demand for infrastructure. As a consequence, the demand for reform of international financial institutions is needed. President Xi Jinping emphasized the desire of stabilizing the world economy through multilateral cooperation. Moreover, while deepening economic ties with neighboring countries through the OBOR initiative, Beijing intensified the engagement with the Bretton Woods institutions. For many years, China has denounced the failure of the international financial institutions that have not recognized China's weight in the global economy. According to the Foreign Policy Analysis theory, domestic situations spill over to foreign policy, conditioning and constraining it. It was only in February 2017 the momentum in which the Chinese President, Xi Jinping, underlined the new country's approach towards international relations namely the "two guides" policy (两个引导 *lianggeyindao*) regarding the new world order and global security. Many initiatives have been established since the Leader took office at the end of 2012. Apart from the AIIB, the new Silk Road Fund was announced, an investment fund established in 2014 with the support of the State Administration of Foreign Exchange (SAFE), China Investment Corporation, Export-Import Bank of China and China Development Bank; moreover, also think tanks such as the Silk Road and the Silk Road Think Tanks Alliance (SiLKS) were found. Furthermore, all these new initiatives are the result of a new Chinese approach to the world. China is also pursuing new neighboring policies such as the RCEP, Regional Common Economic Partnership. The modern neighboring diplomacy within regional strategies has increased the legitimacy of China at a regional level, for example, with ASEAN+3 or the Shanghai Cooperation Organization. According to the words of Xi, it is possible to have a clear understanding of how China is willing to reform the international system, going beyond the world order dominated by the West. The new China-led initiatives and organizations, i.e., the BRI and the AIIB, are deeply connected to the CCP ideational narrative in global politics. In more detail, there can be unraveled precise ideational origins behind the newly designed initiatives. The Fifth Generation of Leaders has developed new concepts such as China Dream, a New Type of Great Power Relations and a New Type of International Institutions. China is becoming a proactive player in the global order, and with the advent of Xi Jinping coming to power in November 2012, Chinese foreign policy has changed according to the main priorities of the country. The Chinese president has fostered the idea of 奋发有为 (*fenfa you wei*) striving for achievements. One of the reasons for the

success of China's new role in global governance can be detected in the attention that the country arose worldwide. The most important example is the concept of China Dream, which is a legacy of the past and is intertwined with another fundamental concept, i.e., the *Tianxia* system (all under heaven). Moreover, the idea of Xi Jinping to build a new type of international relations is at the core of China's foreign policy narrative and public diplomacy. The program for a new kind of international relations has to build win-win cooperation politically, economically, and culturally also with a focus on security issues. So, the policies China will pursue in the next years will be the key not only for the country itself but also for other countries worldwide. The ability of China remains to find a balance between the Chinese interests in international affairs and the interests of other countries in this sphere.

The motivations behind the AIIB can be explained in the context of the One Belt One Road 一带一路 (*yidaiyilu*) or also called the Belt and Road Initiative which was born as an initiative to boost multilateralism, bringing win-win progress and cooperation. This is an opportunity to stimulate the economies of China and the countries involved in the BRI, such as Myanmar, Cambodia, Vietnam and so on. The motivations under this project lie in the guidelines of the new domestic and foreign policy objectives. It appears that Chinese strategic thinkers advocated a new strategy in order to counterbalance rising tensions in the Pacific region with the United States and Japan. Africa is benefitting from this cooperation with China through the aid of the latter to the former. The OBOR initiative, known as the Silk Road Economic Belt and the Twenty-first century Maritime Silk Road, was proposed by leader Xi Jinping during a visit in Kazakhstan and Indonesia in September and October 2013. It can be defined as a multi-level initiative of economic diplomacy. China promotes the One Belt One Road as a win-win initiative, bringing overall global economic growth, one of the most critical worldwide initiatives so far that will bring prosperity and peace. The principles are in line with the purposes of the UN Charter and the Five Principles of Peaceful Coexistence.

President Xi and Premier Li Keqiang addressed the project of the AIIB in 2013 during their visit to Southeast Asia. From that moment, the shaping of the Bank started to develop. The Articles entered into force on the 25th December 2015, and 17 Signatories have deposited instruments of ratifications. The initiative was also part of China's 13th Five-Year plan, which started in 2016. The Asian Infrastructure Investment Bank aims to foster connectivity and help develop infrastructure in member states which are not able



to meet the infrastructural challenges in Asia. The AIIB suits the overall Chinese strategy, and now that China has evolved into a global economic power, there is more concern of domestic and international players in its decision-making. Different from the United States and the rest of the world, the Chinese political-economic system is unique. As a matter of fact, the Chinese system is a hybrid one, which is compatible with the global financial system, and since the China model is a hybrid one, the AIIB follows this model.

Moreover, the AIIB borrows the experience of the World Bank and ADB since many former World Bank and ADB employees' have been advising the Chinese government over the AIIB. The AIIB was officially launched in January 2016 after 27 months of preparation. Notwithstanding the good Chinese intentions to build through development, mutual respect, and win-win cooperation, the AIIB was initially seen more of a challenge. However, after more than two years of operations, it managed to affirm in the international arena also being backed and financially supported by western founding members. The membership has risen from the announcement in 2013 to these days. The growing number of members is a positive achievement for the China-proposed Bank. Not only developing countries participated in the initiative but also developed countries from Europe. This positive outcome has attracted more countries from the beginning, although some US pressures have risen, especially toward the UK, which was the first European country to adhere to the initiative.

### **Chapter three: How regional and non-regional actors responded?**

In 2015, fourteen of the 28 EU states became founder members of the Bank. Not only significant players such as the UK, France, and Germany, but also smaller states such as Denmark, Luxembourg, and Malta decided to take part in the initiative. Following the EU member countries response to the project also some NATO members joined the AIIB. Only Germany and France, major players in NATO after the US, adhered to the initiative despite the contrary opinion of the US. The United States and Japan are both absent since they perceived the project as a loss of power from their perspectives. Although the initial proposal was to prioritize the Association of Southeast Asian region (ASEAN) member countries to foster ties and deepen connectivity between China and ASEAN economies, later Xi Jinping highlighted the willingness to include as many countries as possible from three continents: Asia, Africa, and Europe. The consensus has

not been unanimous; however, the success has been widely accepted. The membership has risen from 57 to -at the time of writing- 97, including both regional and non-regional countries, developing and developed ones. The growing number of members is a positive achievement for the China-proposed Bank. Not only developing countries participated in the initiative but also developed countries from Europe. Another factor ensures more degree of influence from European and other countries, of the 12-member board of directors, about 30% went to non-regional members.

Regarding the case of India joining the AIIB and Sino-Indian ties, India and China have an interesting relationship, sometimes quite challenging including some land disputes. They both are over a billion people; they have fast-growing economies, and both play highly active roles within their institutions. India is such an essential player in the AIIB, and this demonstrates that China is serious in not willing to politicize the institution, and it genuinely contributes to infrastructure in a way that was impossible before. Moreover, being an inclusive institution, again China is serious about a rule-based system through the AIIB, and the countries should be welcoming.

India is not a member of China's Belt and Road Initiative yet, however, New Delhi is participating in the AIIB and signed up to be a founding member of it in 2014. Today India is the most frequent recipient country of infrastructure projects from the Bank and the second largest shareholding in the Bank after China. India has infrastructure needs that can be addressed by the AIIB which already is conceived as a valuable source to fill the infrastructure gap. Moreover, another reason why India decided to join the AIIB, was linked to the fact that the World Bank in 2013 imposed rules and restrictions on loans for projects with a substantial ecological impact. India is still a developing country and an emerging economy which relies on coal. For this reason, many projects proposed to the WB could have been rejected. In this regard, the AIIB can prove to be the ingredient that complements the other financial institutions and fills the gap whenever it is possible.

Moreover, the case of the UK was analyzed. Despite US pressures, the United Kingdom decided to join the AIIB as a founding member in 2015. Among countries that form the G7 (Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States), the UK was the first country to join the AIIB. The adherence of both developing and developed countries to the AIIB was a factor of success for the new Bank. The Chancellor of the Exchequer for the UK, Philip Hammond, has expressed the strong support the UK will give to the AIIB' mission to address the infrastructure gap that currently affects Asia. The UK would contribute \$50 million to AIIB's Project

Preparation Special Fund. Moreover, the UK is actively influencing the AIIB from the inside, contributing with expertise and technical assistance.

According to an interview with the First Secretary of Financial Policy from the British Embassy in Beijing on April 20, 2019 regarding the UK's role in the AIIB there are a couple of things to underline: one is that the UK is a shareholder of the AIIB and is also going to be the first country in the world to contribute to the AIIB's Special Fund. The Special Fund is a technical assistance facility that will help on project preparation, how to get infrastructure projects into place when they can reach financial and private capital, as well as Multilateral Development Bank capital, so it is as a way through the AIIB to take infrastructure projects and make them effective according to best practice and standards. Particularly from an environmental and social perspective, the UK helps ensure that the infrastructure is going to contribute to economic development that will be sustainable in the long term. The Special Fund is something on which the UK has invested in both from a commercial and a sustainable point of view. Another way the UK believes it can be influential in the AIIB is supporting sustainable infrastructure projects by coal reduction policies because they have a strong commitment to coal reduction.

The AIIB has the opportunity to improve the global economic governance, and that's why the UK is engaging, however, if high standards of governance were not ensured the UK would not have joined. On this issue, the UK is a passionate advocate for strong economic governance in the future and the only way to advocate strong governance is to be an active participant in it. The AIIB will help achieve the aims of the Belt and Road; obviously they are approaching the same market, but the AIIB's offer is differentiated. It is active in countries that are not in the Belt and Road, it has open sound procurement, but it is not a vehicle for pure government policies. Since the AIIB is multilateral it cannot be described as a Belt and Road institution.

The ADB is a Japanese-led Development Bank, and China saw a problematic avenue to expand its infrastructure in Asia through this Bank. It is headquartered in Manila, in the Philippines, so it's harder for Chinese to play a creative role. Moreover, China was frustrated for the pace of reform of other MDB's including the World Bank as well, there was an evident frustration on how the system has not adapted to the increasing Chinese economy and a new Multilateral Development Bank was created from scratch in order to reflect the new role. However, China will continue to engage in those other Banks. The AIIB was purely a pragmatic solution to the Chinese new role, and the decision was

taken because the other systems would not have been quick enough and at the same time those proper institutions were not able to adapt in time.

Compared to the AIIB, the NDB is more exclusive and dominated by BRICS countries not only in the governance but also in its purposes.

The two institutions are two different projects, since they have various objects, whereas the AIIB includes Western countries and is based on win-win strategies, the NDB was founded as an alternative to the American ruled Bretton Woods financial institutions. The purposes are different from the ones of the AIIB. The NDB purpose is more restricted. The founding members of the Bank are only BRICS countries; therefore, western countries did not join the Bank. Instead, the AIIB is a constructive forum that sees the participation of Western countries as founding members which with their contributions provided expertise and experience proving once more the multilateral spirit of the AIIB. Also, concerning the election of the President, the two MDB's are different. The NDB's President is elected from one of the founding members leaving no space for other countries voices to be heard. Therefore, for now, there are no prospects for future improvements in the NDB, which once again is a Development Bank which has not proposed new ingredients to reform the international financial architecture.

The African Development Bank has signed Memoranda of Understanding with the Export-Import Bank of China, China Development Bank the Agricultural Bank of China, and the AIIB. Moreover, the two MDBs are following the highest standards regarding level of transparency and openness, and both have the same vision and complement each other. The AIIB is not currently financing projects outside Asia. In the future the AIIB will cooperate with the AfDB in Africa if and only if those projects will benefit also the Asian region. At the moment China Development Bank and China Exim Bank are financing mostly of the projects in Africa.

As a member of the group of development banks, the AIIB has signed several Memorandums on joint cooperation and co-financing with: the African Development Bank, the African Development Fund, the Asian Development Bank, the Eurasian Development Bank, the European Investment Bank, the Inter-American Development Bank and Inter-American Investment Cooperation, the Islamic Development Bank Group (IsDB Group), the New Development Bank and the World Bank Group. There is also an ongoing partnership with private financial institutions in non-governmental sectors. It was also argued that the AIIB is not competing with established MDBs such as the World Bank and the ADB since they both focus on poverty alleviation. For co-financed projects,

the AIIB is currently complementing the existing financial institutions. Moreover, according to Chinese analysts, Asia was lacking in platforms to mobilize financial resources. The World Bank and the Asian Development Bank are just two of many IOs in which countries collaborate in order to provide aids to developing countries. The AIIB has lately also agreed to enhance collaboration with another MDB, the Eurasian Development Bank, in common areas of interest across Eurasia. On December 3, 2018, the MDBs committed on working together in six central key areas to meet the goals of the Paris Agreement, underlining their willingness to commit in order to tackle climate change.

#### **Chapter four: China and the EU: Global economic governance in the framework of the AIIB**

This chapter analyses the case of the AIIB as a tool to enhance global economic governance between China and the EU. Moreover, since the establishment of diplomatic ties between the two countries, there has been an active collaboration on multiple issues.

Since the establishment of diplomatic relations 40 years ago, the China-EU relationship has made progress through joint efforts. Their relationship will be vital and one of the most critical bilateral global relationships of this century. Moreover, China will establish a comprehensive strategic partnership for mutual benefit, since the two sides have been promoting together world peace and joint development.

Initially, the EU looked at the AIIB China-led initiative with suspicion, especially regarding the impact of it in the long term. The initial suspicion regarded to which extent the Bank would have been with Chinese characteristics, à la Chinoise and follow Beijing's agenda. Although China politicians initiated the creation of the AIIB, that did not mean that they have full control over how it is managed, especially considering how the international community responded. Many European countries participated in the AIIB because they foresaw that it was the only way to influence its direction and that the Bank was a possible solution to much-needed infrastructure in poor countries in Asia. Already many MDBs such as the World Bank, ADB, and EBRD have a strong presence in Asia, however, infrastructure needs were not fully met to the high demand in the region.

Since so many European countries were interested in joining the AIIB, the European Union (EU) should further engage with China in order to promote interests, common interests, in the broad context of multilateral institutions. China's global governance policies currently have and will have an impact on the EU. It is vital that

European constituencies work together in order to push and achieve higher standards of accountability and transparency. China's rise in the context of global governance is having a substantial impact both on regional and world architectures. This shift in power distribution from West to East will inevitably have an effect. Many concerns arose regarding China's willingness to establish an international order which is new and not following the existing system laid out after WWII. The EU realized it should engage more and welcome change, but at the same time, it should mitigate risk and be cautious of different ideologies. The AIIB, among the other initiatives of China, will be the protagonist of this shift from a Western-led governance' (*西方治理*) to a more inclusive East-West co-governance' (*东西方共同治理*). However, China's rise will not lead the country to a global hegemonic power, at least according to the Chinese perspective. China has a different view on how the global economic governance (GEG) should be in the future. It's still to be determined what impact the new Chinese-led financial institution will have with regional initiatives launched by the EU, for example the Juncker Plan. Summarized, the EU responded quite well to the establishment of the AIIB and China's attempt to be more involved in world politics. Since several countries have joined, they are trying to positively affect the AIIB policies and provide expertise, influencing development in Asia. However, more cohesive collaboration by the EU member states is needed in order for this Bank to truly benefit the EU. Therefore, the creation of the AIIB is unconsciously forcing the EU to think more as a unified entity than as separate member states which is a good thing for Europe. China is complementing the world order quite nicely. In this regard, the AIIB can draw important lessons from its European counterparts, Europe has two leading regional MDBs: the European Investment Bank (EIB) based in Luxembourg, and the European Bank for Reconstruction and Development (EBRD) headquartered in London. According to the research question of the thesis, it was relevant to give an outlook of the EBRD and the EIB and their ongoing cooperation with the AIIB. In the realm of infrastructure financing, the EU and China are present with multilateral cooperation. China has only recently adopted its theory of global economic governance which is not so distant from the one of the West, however, it has been shaped differently according to the necessities of China. China has to find a role in the global governance architecture. Chinese foreign policy has changed through the years according to the different leaders' aspirations for the country and according to the needs for the development of the country. China's strategy has followed for many years Deng

Xiaoping's vision of "keeping a low profile", which characterized decades of development and avoidance of primary international responsibilities.

Today's perspective is different because the global landscapes and China's role in the world order have changed. The size of the Chinese economy cannot follow the principle of keeping a low profile. As a matter of fact, from Deng Xiaoping's keeping a low profile scenario, Xi Jinping opened a new era with a foreign policy based on 奋发有为 (*fenfa you wei*), or striving for achievements. The latter implies that China should promote reforms within the current system, and at the same time, it should adopt and participate in this mechanism. Another possible scenario is for China to start to establish a new rule system or global economic order in which the country dominates. The role of the state in China is different from the role of the state in Western countries. It plays an overwhelming role in socio-economic affairs, and the country is characterized by a one-party system that considers NGOs and civil society as a threat. As a consequence, Western theories that take into consideration governance without government are not possible to be applied to China's case. The West has generated the current global economic theory. The big question of the twenty-first century is how the future world order will be shaped after China's major initiatives.

The AIIB can in some way jeopardize the rules of the game in Asia, as Asia is in this moment at the heart of China-US rivalry. However, as argued in Chapter 2, at this moment, the AIIB is following the rules, complies with status quo institutions and cooperates with them.

## **Conclusion**

The aim of this work was to analyze the factors that see the AIIB as a complementing ingredient to the existing international financial order. In order to conduct deep research on the topic, I followed the neo-liberal institutionalism theory. The AIIB is a compromise between innovation and well-established principles. The AIIB as a financial institution is institutionalized on multilateralism not only in the constitutional charter but also in the high standards of the Bank. Moreover, it pursues inclusiveness and a consensus approach in the decision-making process. Multilateralism was pursued from the beginning.

It was useful to provide the context in which the AIIB was launched. The current Chinese foreign policy has played an important role in understanding the governance of China. The new concepts developed by the Fifth Generation of Leaders are grandiose and they are also present in the new MDB. This thesis argues that the AIIB project resembles the international norms that discipline and guide the existing Multilateral Development Banks. The Bank has delivered higher efficient projects so far, improving the traditional MDBs. Today's international institutions are not responding efficiently to current challenges. The global system is still linked to the past and fails to satisfy the needs of the current one. In particular, developing countries seek an increase in their influence and seek more recognition in the international arena. However, year by year, developing countries are holding more and more shares of the total global economy. The AIIB as an intergovernmental financial institution mostly aligns with international practices. It was a fascinating case to analyze, and if it will continue to be a success, every country that joined this MDB will benefit from that through spill-over effects.