

FINANCING FOR THE FUTURE

THE VISION FOR THE ASIAN INFRASTRUCTURE INVESTMENT BANK

Jin Liqun

CHINESE President Xi Jinping and Premier Li Keqiang announced the Asian Infrastructure Investment Bank (AIIB) during their respective visits to Southeast Asian countries in October 2013. The AIIB was envisaged to “promote interconnectivity and economic integration in the region.” Citing Asia’s massive and daunting infrastructure needs, China invited the world to join in forming a new multilateral institution that would cooperate with existing Multilateral Development Banks (MDB) in helping to meet this urgent demand. As of the end of June 2015, 57 Prospective Founding Members (PFM) have signaled their interest in joining the AIIB.¹ Fifty PFMs signed the AIIB Articles of Agreement on, June 29th, 2015, in Beijing. The Articles remain open for signature until December 31st, 2015.

GENESIS

In October 2014, representatives from 22 countries signed a Memorandum of Understanding to establish the AIIB, selecting Beijing to host the Bank’s headquarters by consensus. A Multilateral Interim Secretariat responsible for providing technical and professional support and services for the AIIB’s establishment was formed, and I was elected as its Secretary General.

Discussions among PFMs commenced in Kunming, China, in November 2014. At those talks, the Chief Negotiators Meeting (CNM) was established as the forum for PFMs to negotiate and agree on the AIIB’s Articles of Agreement (AOA) and other issues related to the Bank’s establishment. A second CNM in

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Photo: Gulliver Image / Getty Images

President Xi Jinping and other leaders at the October 2014 ceremony establishing the AIIB

Mumbai, India, launched discussions on the draft AOA. This was followed by a third CNM in Almaty, Kazakhstan, in March 2015. By the March 31st, 2015 deadline for submission of membership applications, the number of PFMs had increased to 57, and a fourth CNM was organized in Beijing in April 2015, as a special effort to involve the new PFMs in deliberations on the draft AOA.

The final text of the AOA was adopted by the fifth CNM on May 22nd, 2015 in Singapore.

Throughout the entire process of AOA negotiations, the PFMs had thorough and in-depth discussions on

the AOA in a candid manner, demonstrating their collegiality and spirit of teamwork. It is expected that the AIIB will be operational by the end of 2015.

WHY INFRASTRUCTURE?

Infrastucture investment paves the way for long-term development. Inadequate infrastructure and limited connectivity have long been bottlenecks to growth in Asia. These include both physical links—roads, railways, airports, sea ports, and power grids—as well as telecommunications and intangible links, such as improved policy harmonization, to facilitate the flows of goods, services, and financial resources, as well as customs facilitation.

The development and improvement of production infrastructure in the Asia region is important, as it encourages economic growth, private enterprise, and employment, as well as reinforcing regional connectivity. Infrastructure development enables business activity through improved access to basic services, including a reliable electricity supply, efficient transport systems, clean water supply, access to sanitation services, and modern telecommunications, thus contributing to poverty reduction through broad-based economic and social development.

The rapid growth of Asian economies will also generate opportunities beyond the region, such as expanded markets, and can help spur global economic recovery and growth.

The need for capital for Asian infrastructure is massive, immediate, and acute. In September 2010, the Asian Development Bank Institute published a Working Paper arguing that “by using ‘top-down’ and ‘bottom-up’ approaches,” estimates show that in order to meet growing regional demand “developing countries in Asia require financing of \$776 billion per year for national (\$747 billion) and regional (\$29 billion) infrastructure during 2010–2020.”²

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There is a significant gap between the region’s estimated \$8 trillion infrastructure financing needs over the next decade and the available pool of multilateral and bilateral financing resources. These sums are well beyond the capacity of any one country or even the existing MDBs—notwithstanding the relatively high savings rate in many countries in the Asia region. Although the Asia region is not short of savings, significant challenges remain as to how to more effectively mobilize both public and private sector resources.

Asia’s most urgent need is not the financing itself, but an agile financing mechanism. The AIIB will serve as a specialized platform for infrastructure investment and financing to make

use of the abundant savings within the region. It will cooperate with existing MDBs to promote both infrastructure construction and improvement in Asia by leveraging private sector funding and ensuring reasonable risk allocation with private partners.

Traditionally, countries have funded infrastructure development through a mix of loans from MDBs and domestic budgets, with some private sector financing added to the mix. In the wake of the 2008 financial crisis, government fiscal

constraints multiplied, regulatory regimes tightened, and commercial loans waned. Indeed, according to Goldman Sachs,

infrastructure projects in Asia have been hit particularly hard as remaining lending capacity is allocated to developed economies which provide greater stability. As the European banks withdraw, some regional Asian lenders have taken the opportunity to meet the shortfall in project finance, leveraging their greater access to capital due to stronger deposit bases and less regulatory pressure. However, funding from these new lenders is highly fragile due to their reliance on the deposit base rather than matched long term funding.³

To meet Asia’s burgeoning infrastructure demand, government finance, multilateral assistance, and private capital must be mobilized. Against this backdrop, the AIIB will rise to the challenge. The Bank’s resources will significantly increase the pool of multilateral development support available to regional economies.

WHY THE AIIB?

What is the rationale for a new MDB? This question was raised repeatedly when each new MDB was established during the last half century. For instance, the Asian Development Bank (ADB) was established in the 1960s to supplement the World Bank’s development efforts in the Asia region. Today, the ADB is an impor-

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tant player and partner in promoting economic and social development for public and private investors in this region. In Europe, the European Bank for Reconstruction and Development (EBRD) was created to meet the urgent needs of countries transitioning to a market economy. Other multilateral banks, including the African Development Bank, the Black Sea Development Bank, the Corporacion Andina de Fomento, the European Investment Bank (EIB), the Inter-American Development Bank, the Islamic Development Bank, and the Nordic Bank also have individualized mandates. A development institution

will never be superfluous as long as it can find its niche and contribute positively to growth and development.

The AIIB, as a new multilateral development financing platform committed to supporting infrastructure and interconnectivity development in Asia, is unique in concept and operations. It will be dedicated to helping Asian countries grow with equity, quality, and harmony—harmony with fellow citizens and neighboring countries, and harmony with nature.

The Bretton Woods institutions—the International Monetary Fund and the World Bank, created seven decades ago, and the ADB, now pre-

paring to celebrate its 50th anniversary—have contributed substantially to global and regional economic and social development. Their experiences are noteworthy and their legacy is invaluable. These banks have a strong track record and have continued to achieve remarkable results over time.

Their successes have fostered growth and development, reduced poverty, and helped to shape the Asia region as we know it today.

However, they were all designed in a different era and against a different historical backdrop. As they have each evolved over time, they have also faced challenges in meeting the needs of their members under new circumstances, with each institution embarking on its own reform process to meet these challenges. The AIIB has a fresh slate. Its founding members have a once in a lifetime opportunity to design a streamlined, results- and outcomes-focused organization that is built on the principles of transparency, openness, independence, and accountability.

WHAT'S NEW?

The AIIB's shareholders, through their full hands-on engagement in its establishment process, are uniquely poised to ensure that the AIIB's governance, organization, and policy framework benefit from the lessons and reform efforts of existing MDBs, while

incorporating global best practices. The World Bank, IMF, ADB, EBRD, EIB, the International Fund for Agriculture and Development, and private sector organizations continue to be generous in sharing their knowledge with the AIIB's PFMs as they consider institutional design and policy issues.

In creating a new institution whilst building on institutional legacies that in some cases go back nearly seven decades, the AIIB's owners are using this existing knowledge to shape systems, policies, and procedures in order to enhance efficiency, promote cost effectiveness, and achieve measurable results. Their hands-on participation will ensure appropriate oversight mechanisms are put in place and implemented. Also, intensive shareholder involvement in the

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AIIB's establishment process provides a deep and durable base for its enhanced development effectiveness.

HOW WILL IT OPERATE?

Together, the AIIB's shareholders are working to ensure that the Bank operates as a lean, clean, and green organization.

International experts are helping the Secretariat to develop policies built on global best practice and lessons of experience. The AIIB will have a small workforce of experienced specialists in a variety of fields, and will work in an efficient and timely manner. The system is being designed to avoid the creation of red tape. Cost effectiveness will underpin all the Bank's operations. The AIIB will have zero tolerance for corruption and fraud.

The AIIB is committed to the principles of sustainable development in the conceptualization, design, and implementation of its investment activities. It recognizes the importance of managing environmental and social risks as an integral part of infrastructure operations. With support from international experts, the Secretariat has

initiated a process to develop an environmental and social policy framework to ensure the integration of these principles into its operations. This framework is being designed in consultation with shareholders and other stakeholders. The final policy framework will be approved by the AIIB's Board of Directors.

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Similarly, on procurement, the AIIB will draw on current best international procurement practices to develop an appropriate procurement policy framework to govern its operations. The core procurement principles will be based on economy, efficiency, value for money, fairness, transparency, and integrity. Again, the policy framework will be approved by Board of Directors.

Good governance is key to success. The AIIB's ultimate success and credibility depend upon its ability to enact sound governance policies, practices, and mechanisms, as well as to ensure their effective implementation. It will not only develop policies that are sound and principled, but will also strive to foster a strong implementation culture within the Bank, as well as supporting rigorous policy implementation.

Building on the principles of transparency and accountability, the AIIB will install effective oversight mechanisms to ensure compliance with its Board-approved policies, promote integrity in the conduct and performance of its management and staff, and prevent and redress fraud and corruption in operational activities.

HOW WILL IT COOPERATE?

The AIIB will cooperate with existing MDBs. Regional demand for infrastructure finance is significant, and there is ample room for multilateral and private institutions to support regional clients. The AIIB's firm intention—strongly endorsed by its PFMs—is to be a sound, collegial, and reliable partner to existing MDBs. Its activities will complement and supplement existing MDB programs.

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In its design, the AIIB has been learning from the practical experience of existing institutions, through workshops, MDB staff exchanges and secondments, policy briefings, and informal advisory support. For instance, a March 2015 Workshop in Beijing brought together specialists from MDBs, think tanks, and the private sector to share their expertise with the AIIB's future shareholders on governance, environmental, social, and procurement policies.

In its operations, the AIIB will continue to learn from its clients, shareholders, and other stakeholders. Once up-and-running, the AIIB will have close on-the-ground cooperation with other financing institutions on sector based issues and opportunities. The AIIB expects to co-finance projects with MDBs and envisions possible opportunities to partner on joint analytical work and/or technical assistance once the Bank's teams are fully operational.

WHAT WILL IT OFFER?

As a modern infrastructure financing institution, the AIIB aims to deliver:

Investment: by providing financial resources, cutting-edge knowledge, and global best practice expertise, the AIIB will support the development and operation of new and existing infra-

structure in a principled, cost effective, and timely manner, while delivering value-for-money and fit-for-purpose financing.

Innovation: through partnerships with government, the private sector, and civil society, the AIIB will encourage innovative approaches to help meet Asia's infrastructure challenges.

Integration: the AIIB will ensure integration of environmental and social

sustainability as a core element in its policies, plans, and operations.

Integrity: the AIIB will operate in a transparent manner and incorporate integrity as a core principle.

Insight: the AIIB will aim to provide insight on the emerging issues and key trends that will drive infrastructure and interconnectivity in Asia.

CHINA AND THE AIIB

Although the conceptualization of the AIIB grew from China's initiative, the AIIB is a bank for Asia, owned by all of its founding members from across the world. PFMs from five continents have come together to jointly build a robust and durable institution that uses the best historical experience and global best practice to pave new ground in designing effective and efficient policies and procedures to realize its vision.

The AIIB is an institution dedicated to fostering economic development, creating wealth, and improving regional connectivity. It will focus on regional cooperation through win-win solutions. The AIIB's shareholding structure, with Asian regional member majority ownership, ensures that the voice of all its members—small and large alike—will be heard. Good and transparent governance will be the cornerstone of its foundation and the key to its success.

The AIIB holds great promise to contribute significantly to improving the lives and livelihoods of citizens of the Asia region. The rest of the world will benefit from the spillover of Asia's growth potential and prosperity.

With continuing strong support from its shareholders, it will realize this promise. ●

ENDNOTES

¹ The 57 PFMs are: Australia, Austria, Azerbaijan, Bangladesh, Brazil, Brunei Darussalam, Cambodia, China, Denmark, Egypt, Finland, France, Georgia, Germany, Iceland, India, Indonesia, Iran, Israel, Italy, Jordan, Kazakhstan, Republic of Korea, Kuwait, Kyrgyz Republic, Lao PDR, Luxembourg, Malaysia, Maldives, Malta, Mongolia, Myanmar, Nepal, Netherlands, New Zealand, Norway, Oman, Pakistan, Philippines, Poland, Portugal, Qatar, Russia, Saudi Arabia, Singapore, South Africa, Spain, Sri Lanka, Sweden, Switzerland, Tajikistan, Thailand, Turkey, the United Arab Emirates, the United Kingdom, Uzbekistan, and Vietnam.

² As quoted from the *Abstract of Estimating Demand for Infrastructure in Energy, Transport, Telecommunications, Water and Sanitation in Asia and the Pacific: 2010-2020*, ADBI Working Paper 248 (ed. B. Bhattacharyay).

³ As quoted in *Financing for Infrastructure in Asia*, Goldman Sachs, May 2015.