AIIB Contributions to the Eminent Persons Group (EPG)

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The Asian Infrastructure Investment Bank began operations in 2016 with an anticipated five-year start-up phase focusing on building the institution. During its initial two and half years, the Bank established its basic policy framework, financed its first operations and launched a first group of sectoral strategies. Membership of the Bank grew from 57 to 86. Strategic partnerships with a number of Multilateral Development Bank (MDBs) and related organizations were established. By the end of May 2018, AIIB had financed $4.39 billion for 25 projects.

AIIB's investments in infrastructure are pursuing three thematic priorities that are closely linked to the themes of the EPG symposium: 1) cross-country connectivity (in particular cross-country transport and energy connectivity), 2) sustainable infrastructure (in particular climate change mitigation and adaptation), and 3) private capital mobilization.

The willingness of its member countries to subscribe to $100 billion of share capital to establish AIIB as a new Multilateral Development Bank (MDB), is first and foremost a testimony to the compelling nature of the basic MDB governance, financial, and business model. The creation of AIIB also demonstrates that different countries can take the lead in the establishment on an MDB, building on a tested and well proven basic model.

The establishment of AIIB provides an opportunity to reflect on the lessons of seventy years of MDB experience and draw on those lessons that are relevant for the particular case at hand. Of course, the lessons for creating a new institution to complement the existing system can be very different from lessons for reforming existing institutions. Nevertheless, key lessons drawn from experience and the decisions taken for AIIB are listed here to inform the debate on system reform.

Governance

Shareholder composition of AIIB reflects the regional nature of the Bank--75% of shares are allocated to its regional members and 25% to its non-regional members. Within these two blocks, shares were offered to founding members according to their relative economic weight. The resulting shareholding composition is therefore reflective of current economic realities.

AIIB does not distinguish between borrowing and non-borrowing members. Nevertheless, AIIB financing is relatively more attractive to its members with less or no market access, however, AIIB does not have the concept of graduation and can lend to UMICs and HICs. It therefore avoids a bifurcation of its shareholders.

AIIB's Board of Directors is a non-resident, non-executive Board that routinely meets once a quarter for several days, complemented by video meetings on an as-needed basis. Early experience with this model has been positive, combining efficiency with strong shareholder engagement and oversight.

AIIB's Articles of Agreement foresee the delegation of authority for approval of projects to the Bank's President. A new "Accountability Framework" related to this delegation was approved in April 2018, which will be implemented gradually. It is expected that this delegation will allow the Board to focus on its critical policy and strategy setting role. It will establish stronger oversight by the Board and more accountability of management and avoid an excessive focus of the Bank on project approval as opposed to project selection, preparation, implementation, and results.

Any special or grant funds in AIIB are funds of AIIB that are overseen by the same Board, managed by the same management and subject to the same policies as AIIB's regular resources. This approach avoids the fragmentation of institutional governance that can occur with the administration of trust funds or similar arrangements under separate governance.

Finance

AIIB's first years of operation show brisk demand from all of its potential client groups. The early experience validates the premise of very large, excess, unmet demand for the services and in particular the financing from MDBs, which is documented in various studies of infrastructure finance needs worldwide and in particular in the Asia Region.

AIIB's financial model is based on financial sustainability. It does not rely on continuous inflows of concessional finance or recapitalization. AIIB is mandated to use its net income to grow its capital base.

While AIIB is currently well capitalized, its capital is ultimately limited compared to the financing needs of its members. Therefore, AIIB is from the beginning focusing on the mobilization of private capital in addition to the deployment of its own balance sheet. AIIB participates in the various initiatives and working groups among the MDBs that promote the effective mobilization of private capital, in particular for infrastructure. In 2017, the total amount of private cofinancing with AIIB was $561 million.

AIIB recognizes that many infrastructure projects involve public and private actors as well as sub-sovereign entities. AIIB serves all its clients with one balance sheet and one staff but differentiated financial instruments (sovereign-backed versus non-sovereign backed financing). This approach promises to provide seamless services to the spectrum of clients from pure public to pure private, including semi-private and sub-sovereign.

Business Model

AIIB intends to build a business model that is focused on infrastructure project finance. It does not intend to offer, and is not resourced to provide, policy lending or wider range of advisory and other services offered by some of its peers.

As a newcomer, AIIB recognizes the existence of many actors with far ranging capacities relevant for AIIB's mandate, including government entities, private companies, financial institutions, consulting companies, think tanks, academic institutions, civil society organizations, bilateral agencies, and of course other IFIs/MDBs. Rather than duplicate the capacity of existing institutions, AIIB aims to establish a lean business model with limited in-house staff and capacity but closely networked with other institutions through partnerships and outsourced service arrangements.

AIIB's operational policies allow the efficient co-financing with other partners who apply similar, though not necessarily identical, policies on environmental, social, governance (ESG) and other aspects of project due diligence. AIIB is also able to rely on country policies and systems where they achieve the objectives set by AIIB's ESG policies.

AIIB has already entered various cofinancing arrangements with the World Bank, IFC, EBRD, ADB, and EIB. In many of the cofinanced projects, clients benefit from the technical capacity of, and project preparation support provided by, the partner MDB complemented by the additional financial capacity of AIIB. AIIB has also benefited from technical assistance provided by peer institutions and by staff exchanges with them. In many ways, the young history of AIIB is already demonstrating a good example of the MDBs operating jointly as a system that serves its clients better than individual institutions would be able to do on their own.

Finally, we would like to offer a few suggestions for further work of the EPG.

While much discussion has focused on the better working of the MDBs as a system from the perspective of their shareholders and Boards, a different, possibly very productive, focus would be on the effectiveness of the MDB system from the perspective of their sovereign and non-sovereign clients. AIIB has benefitted from numerous consultations with its current or potential clients and learnt a great deal about their expectations. We would recommend that the EPG conduct similar client consultations. We would expect that policy harmonization and compatibility, use of country systems, flexibility, which may sometimes contradict the desire to standardize, and overall orientation of MDB programs along country priorities would be some of the themes that might emerge from such consultations.

We welcome and participate in the multiple current discussions on private capital mobilization by the MDBs. This discussion is focused on the instruments and actions by MDBs even though the more binding constraints often lie in the availability of well structured ("bankable") projects. Even the efforts to increase international support for project preparation may not adequately address the underlying root causes in many countries. Ultimately, each country itself and its different stakeholders hold the key to overcoming institutional (rather than technical and financial) constraints to the preparation of bankable projects. This relates to the previously mentioned importance of reviewing the effectiveness of the MDB system from the perspective of its country clients and their efforts to build effective institutions in their own countries.

The role of concessional finance in the MDBs merits closer review. The wide range of governance and financial models currently deployed and their effectiveness and results deserves careful analysis. This relates to the way in which different models combine or pursue separately concessional financing for global objectives with non-concessional finance for national or local objectives. In particular, multiple concessional finance (trust) funds under separate governance arrangements may serve well the objectives of individual contributors and recipients but can weaken the ability to manage coherently the host MDB, let alone the MDBs as a system.