

Evaluation of Recent Development of the AIIB: The 2nd Annual Meeting of the AIIB Held in Korea and its Implications

LEE Hyuntai Research Fellow, China Team, Department of Northeast Asian Economies (htlee@kiep.go.kr)

KIM Junyoung Researcher, International Cooperation for Korean Unification Team, Department of Northeast Asian Economies (junyoung@kiep.go.kr)

OH Yunmi Researcher, China Team, Department of Northeast Asian Economies (ymoh@kiep.go.kr)

I. Overview

On June 16-18, 2017, the Asian Infrastructure Investment Bank (AIIB) held its 2nd Annual Meeting in Jeju Island, Korea under the theme of “Sustainable Infrastructure.” Representatives of the Korean government, including President Moon Jae-in of the Republic of Korea, and leaders of the AIIB, including President Jin Lique and representatives of 80 member countries, attended the meeting to evaluate the progress made up to now and to discuss the future development of the AIIB. In addition, various seminars were held on the key issues of the AIIB, such as sustainable infrastructure, improved global governance, financing infrastructure in Asia, and building public trust. Korea successfully hosted the 2nd AIIB Annual Meeting, which was held outside of China for the first time and served as an opportunity to further improve its standing as a core member of the AIIB. As the AIIB is likely to further develop following this year’s Annual Meeting in the Republic of Korea, this paper analyzes the contents of the Annual Meeting and recent development of the AIIB, and goes on to suggest future prospects and implications for Korea.

II. Recent Development

After its launch in January 2016, the AIIB is evaluated to have achieved quite rapid development through the approval of many projects, expansion of member countries, and strengthened cooperation with other organizations. Since its inception, it has been carrying out its projects quickly, with a total of 26 projects to date (16 approved projects, 10 proposed projects).

At the 2nd Annual Meeting, membership was approved for Argentina, Tonga and Madagascar, expanding the number of AIIB members to 80 countries and exceeding the Asian Development Bank (ADB), which has 67 members, in terms of membership.¹ Meanwhile, the AIIB is strengthening cooperation with existing international financial institutions such as the World Bank (WB), ADB, Inter-American Development Bank (IDB), New Development Bank (NDB) and International Finance Corporation (IFC) in terms of joint

¹ AIIB President Jin Lique (金立群) expects the number of member states to increase to 85 countries by the end of 2017. (Source: “一带一路” 国际合作高峰论坛)

projects, human exchange, and knowledge sharing. These cooperation projects are helping the AIIB to smoothly integrate into the existing international financial order.²

To take a more specific look at the projects that have been carried out, the AIIB has approved a total of US\$ 2,499 million in loans for 16 projects in the fields of transportation, energy, and urban infrastructure, among others. While only four projects (US\$ 509 million) had been approved before the 1st Annual Meeting, 12 projects (US\$ 1,990 million) were newly approved following the Annual Meeting, showing an increase of 3.9 times in terms of total amount approved. This reflects how the staff at the AIIB has been able to carry out expedient screening for prospective projects, unlike the existing MDBs, which generally require more than two years to approve a project.

Many AIIB-funded projects are concentrated in the fields of energy and transportation, with a relatively large number approved in the energy sector after the first Annual Meeting. Region-wise, there is much support for infrastructure projects in South Asia, Central Asia and Southeast Asia.

Most of the projects are being conducted as co-financed projects with MDBs such as the ADB, WB and European Bank for Reconstruction and Development (EBRD). Among the 16 approved projects, there are only four stand-alone projects, taking place in Bangladesh (Distribution System Upgrade and Expansion Project), Oman (Railway System Preparation Project, Duqm Port Commercial

Terminal and Operational Zone Development Project), and India (India Infrastructure Fund). Currently the AIIB has only 100 staff members, meaning it lacks the internal capability to conduct these projects independently. Therefore, the AIIB is seeking to mitigate risk, acquire know-how in its business and operations and enhance international public confidence through cooperation with existing MDBs.

Meanwhile, 10 projects (US\$ 1,949 million) are currently under review as of June 20, 2017. These 10 projects total an amount of US\$ 8,481 million, of which the AIIB will fund approximately US\$ 1,949 million, or around 23%, of these loans. The projects are mostly in the sectors of energy, transportation, and urban infrastructures, with a total of six projects in India, and most of the proposed projects planned to be co-financed with other MDBs.

In terms of the AIIB's strategy, it has selected three thematic priorities and four institutional goals, and is making full-scale efforts to establish strategies for each infrastructure sector, form external financing, hire and develop talent. The AIIB's three thematic priorities are: ① Sustainable Infrastructure, ② Cross Border Connectivity, and ③ Private Capital Mobilization.³ Also, the following four initiatives have been set as its goals for institutional development: ① Sharpening the Bank's Strategic Focus and Shaping its Corporate Brand, ② Scaling Up Support to Clients and Refining the Programming Approach, ③ Bolstering Financial Stability and Paving the Way for Market Access, and ④ Continuing Institution Building.⁴

² See LEE Hyun-Tai, KIM Junyoung. 2016. "AIIB Development: Forecast and Implications" and GU Bin. 2017. "Chinese Multilateralism in the AIIB." *Journal of International Economic Law*. 137-158.

³ See 2017 Business Plan and Budget Summary (AIIB, 2016 December)

⁴ See Energy Sector Strategy: Sustainable Energy for Asia (AIIB, 2017 June)

The mid- and long-term strategies in the energy sector that the AIIB has established over time were recently approved by its board of directors, while its strategies for other sectors such as transportation and sustainable cities are currently being designed. At present, there are 100 employees, and the AIIB is focusing on recruiting high-level international financial personnel to strengthen its internal capabilities, while also cultivating young talent through programs such as the Young Professional Program.

Meanwhile, in addition to China, which has led the AIIB from its inception, the US and Japan, while critical toward the AIIB in the past are now showing interest in the strategies of the AIIB and the Belt and Road Initiative and shifting toward a proactive stance. China is engaging in active discussions on the development and utilization of the AIIB, its common points with and differentiation from existing MDBs, and the responses and policies of other countries regarding the AIIB and the Belt and Road Initiative. Interestingly, US President Trump is hinting at cooperation with China on the Belt and Road strategy, emphasizing economic cooperation with China following the US-China summit in April. In addition, senior Japanese officials are calling for Japan to join the AIIB, and there is the possibility that Prime Minister Abe could announce a decision to join the AIIB in the near future.

III. The 2nd Annual Meeting

The 2nd AIIB Annual Meeting (hereinafter “the Annual Meeting”) was held in the Republic of Korea as an international forum to evaluate the operations of the AIIB and present and discuss short and long-term strategies and challenges. The Annual Meeting consisted of

the Opening Ceremony, the 1st and 2nd Governors Business Session, AIIB Strategy Briefing and a session on the AIIB’s investment program and its investment policies and procedures. The Meeting also included the Governors’ Seminars, Banks’ Seminars, Seminars I – IV on several topics such as “Financing Infrastructure in Asia,” the India Seminar, Business Session, Infrastructure Exhibition Tour, a press reception by the President and the Host Country Dinner.

At the Annual Meeting, the AIIB particularly emphasized the keyword “Lean (efficient)” in its business operations, presenting the core principles of its short- to long-term strategy as “Lean (efficient), Clean (ethical) and Green (environment-friendly)” operations. The “Lean” principle refers to how the AIIB, unlike other MDBs, does not have a standing board of directors, and instead conducts its business promptly through various working groups, trying to eliminate bureaucracy through organic cooperation with governments, institutions, enterprises, think tanks and NGOs. In addition, the AIIB has set a goal of doubling the total annual amount of its business by ensuring efficiency in its business operations (from \$ 2.5 billion this year to \$ 5 billion next year). The principle of “Clean” emphasizes the importance of zero-tolerance when it comes to corruption-related activities, and the AIIB is also emphasizing its focus on environment-friendly infrastructure while faithfully implementing the Paris Agreement through the “Green” principle.

Meanwhile, when it comes to the AIIB’s investment operations, its program includes the expansion of non-sovereign backed financing projects and equity investment plans, while also emphasizing that profitability of business is important. It introduced a single balance sheet incorporating both sovereign-backed financing projects and non-sovereign backed

financing projects (including private businesses) and diversified financing, but stated that it would carry out business in a thoroughly commercial context. At present, most projects are conducted with sovereign backed financing, but the AIIB has expressed its intention to increase non-sovereign backed financing projects in the future.

For example, the AIIB Investment Operations Department proposed a road-map for future plans of the AIIB's non-sovereign backed financing. This is scheduled for: Launch in 3Q 2016→ Establishing the fund strategy in 4Q 2016→ Initiating the stand-alone projects in 2Q 2017→ Establishing the syndicated loans through co-financing in 3Q 2017→ Initiating the direct equity investments in 4Q 2017→ Enhancing the investment tools in 2018→ Adopting major international currencies in 2019 and local currencies in 2020. In addition, the AIIB has gradually expanded its business scope to advise and arrange private capital infrastructure investment, and set its goal to become a global MDB that can lead the infrastructure financial market in the future.

In-depth discussions took place at various seminars, with the AIIB International Advisors panel, international organizations such as other MDBs, and experts from around the world participating in AIIB-related topics. The AIIB organized sessions on “Sustainable Infrastructure,” “Improved Global Governance,” “Financing Infrastructure in Asia,” “Building Public Trust in Infrastructure Investment,” while the chair country Korea organized sessions on “The Era of the 4th Industrial Revolution and Infrastructure,” “Bridging the Gap in Infrastructure Financing,” “Challenges and Breakthroughs in Promoting New & Renewable Energy Infrastructure in Asia,” and “Partnership in Promoting Infrastructure Invest-

ment in Asia.”

Among the seminars, the sessions on “Sustainable Infrastructure” and “Improved Global Governance” deserved particular attention. In these seminars, the invited former and present high-ranking officials of other MDBs and top experts in the international community discussed that the AIIB should actively implement a 21st century MDB model in the global governance paradigm and its MDB operations. In the current situation, where the existing MDBs are being criticized for their oversized organizations, bureaucratic bloating, and Western domination, there has been a focus on whether the new MDB, AIIB, can build a new MDB model different from the existing MDBs. There has been a call for the AIIB to grow into a 21st century type of MDB in terms of the operation of its organization, business execution, and public trust.

Meanwhile, Korea successfully hosted the first annual meeting held outside of China and raised its international status. It succeeded in reinforcing its position as a key member of the AIIB by thoroughly preparing for smooth operations through its relevant ministries, such as the preparatory planning committee for the Annual Meeting established at the Ministry of Strategy and Finance and other careful preparations made by the Jeju Special Self-Governing Province.

Throughout the proceedings, Korea demonstrated a great deal of interest from its government and private sector, as shown by the participation of President Moon Jae-in and Deputy Prime Minister and Minister of Strategy and Finance Kim Dong-yeon. At the opening ceremony, President Moon Jae-in emphasized the importance of infrastructure investment for sustainable growth, inclusive growth and job creation, and voiced his intention to

actively share the development experience of Korea with Asian developing countries and to act as a partner for development. In addition, as the chairman of the Annual Meeting, Deputy Prime Minister Kim Dong-yeon expressed his intention to support the AIIB, emphasizing the harmonization of economy and environment, harmonization with government policy, and the harmony of public and private sectors.

IV. Forecast and Implications

The AIIB is expected to respond to new global challenges such as sustainable development, climate change, the 4th industrial revolution, and the digital economy by constructing infrastructures, while aligning its operations with the core principles of a lean (efficient), clean (ethical) and green (environment-friendly) organization, thus aiming to develop into a new type of MDB appropriate for the 21st century.

However, in order to develop into such a 21st century MDB model, the AIIB will have to overcome many difficulties. First, the AIIB needs to handle the internal capability problem. Currently, there are concerns about whether the AIIB has the capability to implement new global issues such as sustainable development, climate change, the 4th industrial revolution, and the digital economy in real infrastructure projects with such a small number of employees. Second, the AIIB should overcome the profitability problem. As an investment bank the AIIB must constantly struggle to sustain its growth because there are not many infrastructure projects in developing countries that guarantee high returns. Third, there are the institutional limitations. Currently, the AIIB's organizational structure, policies, and operational procedures are similar to those of existing MDBs, and many of its employees are former

members of the existing MDBs. Therefore there is the possibility that the AIIB could change into an organization similar to the existing MDBs as it grows in size. Fourth, it will be important to control the potential conflict breaking out between member states. There is a possibility that competition and conflict will escalate among the member countries that require funding from the AIIB. Fifth, there is the issue of China's influence. The question of how China, as the largest shareholder, exercises its influence will be a measure of AIIB's progress toward a truly international cooperation body.

While the AIIB has these challenges to overcome, it is expected that the bank will steadily progress over the next five years under full support by President Xi Jinping and the Chinese leadership.⁵ However, the AIIB is likely to continue to grapple with how to treat the global issues that are emerging from outside and the internal problems that the existing MDBs face. It is also expected that discussions will be held on how to upgrade the existing Bretton Woods system as China-led international financial institutions such as the AIIB, NDB and Silk Road Fund continue to grow.

In line with the development of the AIIB, Korea should develop a new infrastructure model that incorporates new global issues such as the 4th industrial revolution, climate change, the digital economy, and sustainable development, proactively present this to the AIIB and encourage the participation of Korean companies in these business projects. In addition, based on its experience with successfully leading infrastructure investments in the past, Korea needs to actively develop infrastructure development projects that contribute to inclusive

⁵ Renmin University IMI interview, conducted in March 2017

growth, such as projects that contribute to regional balanced growth, high-quality job creation, and social integration in Asian developing countries, and actively present these to the AIIB. It would also be possible for Korean local governments to utilize their networks of exchange and cooperation with cities and regions in Asian developing countries to jointly develop local infrastructures in these countries. Finally, Korea should nurture international financial talent and support policy and academic research related to the AIIB, Belt and Road Initiative and Asian infrastructure market, and through this position Korea could consider acting as a network hub of related research and information. 