The Emergence of the Asian Infrastructure Investment Bank

- The very rational choice of legitimacy

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Abstract

Development finance has never been a more vibrant and interesting field of study. With the economic and political rise of China, and the recent establishment of the Asian Infrastructure Investment Bank (AIIB), international multilateral development banking is back on the high-level political agenda. In our research question we ask, what are some of the key factors that led to the emergence of the AIIB, and what role these factors played in the emergence and design of the institution? Furthermore, we ask who benefit from the AIIB and what are some of the key barriers for private capital to enter into financing of infrastructure projects in developing countries?

We conducted a disciplined interpretive two-stage case study based on critical realism. New Institutionalism has been our theoretical frame for answering the first part of our research question. To answer who benefits in stage II, we applied Susan Strange's four pillars framework to identify structural power change. The key factors we focused on were based on three selection criteria. 1) Uneven Representation in current institutions, 2) Infrastructure Finance Gap in Asia, and 3) Chinese Capital Capacity. Our analysis of these factors revealed that the emergence of the AIIB was a very rational choice by China, and furthermore an important stepping up the latter in development finance in regards to be perceived as a legitimate actor. The design of the AIIB is a balancing of domestic interests and structural and normative pressures from the MDB community. In our Strangeian structural power analysis we concluded that the emergence of the AIIB is benefiting various actors. The European member states have the potential to benefit from an increased demand for their companies expertise. Our analysis revealed that China is the only actor benefiting across all four pillars.

Finally, we identified three major barriers for private capital. 1) Lack of a real infrastructure market caused by poor project development and limited pipeline, 2) complexity in the current guarantee system, which make investors withdraw from investments, and 3) paradigmatic discrepancies between private investors and the MDB community, which complicates cooperation. In the end we discussed the AIIB in relation to Varieties of Capitalism and suggested some further research.

List of Abbreviations

ADB: Asian Development Bank

AgDB: Agriculture Development Bank

AIIB: Asian Infrastructure Investment Bank

AoA: Articles of Agreement

ARC: African Risk Capacity

AU: African Union

BoD: Board of Directors

BoG: Board of Govenors

BRICS: Brazil, Russia, India, China, South Africa

CBS: Copenhagen Business School

CDB: Chinese Development Banl

CME: Cordinated Market Economy

CR: Critical Realism

DIIS: Danish Institute for International Studies

EIB: European Investment Bank

ERBD: European Bank for Reconstruction and Development

ExIm Bank: China ExIm Bank

GDP: Gross Domestic Product

HI: Historical Institutionalism

HPAIR: Harvard Project for Asian and International Relation

IABD: Inter American Development Bank

IBRD: International Bank for Reconstruction and Development

IDA: Internatinal Development Association

IFI: International Finance Institution

IMF: International Monetary Fund

IO: International Organization

IPE: International Political Economy

IR: International Relations

LGFV: Local Government Financing Vehicles

LME: Liberal Market Economy

MDB: Multilateral Development Bank

MNE: Multinational Enterprise

MoFA: Ministry of Foreign Affairs

MoU: Memorandum of Understanding

NDB: New Development Bank

ODI: Overseas Development Institute

PE: Private Equity

PFM: Prospective Founding Members

PPP: Public Private Partnership

RCI: Rational Choice Institutionalism

RMB: Renminbi

SI: Sociological Institutionalism

SOE: State Owned Enterprise

UN: United Nations

VoC: Varieties of Capitalism

VP: Vice President

Table of Contents

1. Introduction

Even though the world is becoming richer and more globalized, developing countries in particular are increasingly facing global challenges that are setting a new context for development and growth. Some of the most impactful challenges to these countries will be climate change, financial crises, economic disparity, global governance failures, geopolitical conflicts, and corruption (Massa & te Wilde, 2011). Many of these issues were originally intended to be mitigated through the involvement of multilateral development banks (MDBs), which is still the case.

The establishment of the Bretton Woods institutions was a landmark in the reshaping of the international finance system, and the development finance system in particular. In subsequent years, regional economic and political groups established their own development institutions. A number of these institutions were created for political reasons, but they also served to address the development challenges related to provision of basic services. Much has happened since, and today the big issue is funding.

The international community is these days struggling to mobilize money from the traditional donor governments for long-term infrastructure investments, and therefore focus are increasingly directed towards the private sector, philanthropic foundations, and emerging donors such as China to fill the infrastructure funding gap (The Guardian, 2016). Unanswered questions are still how we get new models for development finance up and running, and how to incentivize potential investors? And where will new and old development banks fit into the future development landscape?

All these questions are relevant, but the emergence of the Asian Infrastructure Investment Bank (AIIB) deserves our fullest attention, as it might have the most far-reaching consequences for development finance. We have specifically chosen to ask the following research question:

> ***What are some of the key factors that led to the emergence of the AIIB, and what role did these factors play in the emergence and design of the AIIB? Who benefits from the AIIB, and what are the key barriers for private capital in development finance?***

In short, our research question is guided and formulated based on a desire to provide answers to the broader questions; why, how, and who.

Studying the AIIB is important as the institution will affect more than just the development finance field. A successful bank will have long-term consequences for economic growth, development, and security in Asia, but also in regards to multilateralism in general. Furthermore, as China is the architect behind the establishment of the bank, everyone with an interest in international political economy, financial markets, and development such be eager to understand more about this new MDB.

Delimitation

This thesis has made multiple conscious decisions to define a scope that has given a necessary level of data and an ability to make a meaningful contribution. Firstly, we have made a conscious choice about data, where we have chosen to focus on interviews combined with desktop research. We find that this approach suitable in regards to our research questions, as it give us the necessary situational understanding to uncover the underlying mechanisms driving the factors. Existing studies have focused on the quantitative aspect (estimation of finance gap etc.) of the economic features leading to the emergence of the AIIB (Reisen, 2015; Biswas, 2015). This thesis seeks to contribute with a deeper understanding, which is achieved only through qualitative interviews. Moreover, the quality and availability of data from China can be questioned, and we have therefore sought to obtain first-hand data to secure the validity of our observations.

It is important to note that this thesis does not attempt to provide an exhaustive list of factors leading to the emergence of the AIIB. Neither we intend to elaborate and analyze the impact of the AIIB on all involved actors. Instead we prioritize a thorough and detailed assessment of a set of key factors which are carefully chosen. This choice connects to our research contribution, as we desire to create an analysis with great depth and therefore we leave a thorough mapping of all factors up to others.

We have made a conscious choice of our case, and our initial research included both the BRICS Bank (New Development Bank) and the AIIB. The reason for initially including both was that they share similar characteristic in terms of being MDBs led by developing countries. However, through our research process it became apparent that the NDB was less relevant for our study, as it is a more politicized bank and the membership constellation is very narrow. AIIB is interesting as it is the first serious attempt from China to create an institution taking a collaborative approach to address the infrastructure challenges we are currently facing in Asia. This was exactly the type of case we were looking for to conduct a case study.

We will throughout the thesis remind the reader of our delimitations where it is deemed appropriate.

Structure

The thesis will be structured as follows: Firstly, the foundation will be established with sections covering philosophy of science, methods, and research design. Secondly, the background information will provide the reader with the necessary context to follow our analysis. Thirdly, the theoretical frameworks applied in the analysis will be introduced and positioned in relation to our case. Fourthly, the analytical approach will be explained and our two stages of analysis will be presented. Finally, we will discuss the market barriers for private capital and the future implications of the AIIB for development finance before concluding the thesis.

2. Methods

2.1 Philosophy of Science: A Critical Realist Perspective

This thesis will apply a critical realist (CR) philosophy of science. The purpose of this section is to briefly outline the core ideas of CR and how these will be applied in this thesis.

The major ontological view in CR is a realist philosophy of science, embodied by the idea that reality exists without our knowledge of it (Buch-Hansen & Nielsen, 2005: 14; Bhaskar, 1989: 49). It is important to note that it is necessary to expand the idea of a realist philosophy of science in order to outline how CR expands the traditional realist philosophy - also known as an empirical realist perspective. The considerations linked to empirical realism is that reality is defined by structures observable to the human senses. In the critical realist philosophy reality is also seen to be stratified. Stratified means that reality is defined by layers of causal mechanisms, which through interaction creates the reality of everyday life (Buch-Hansen & Nielsen, 2005: 16-18). In order to attempt to clarify this philosophical argument, reality can be divided into three basic layers (Buch-Hansen & Nielsen, 2005: 22-24).

- **The Empirical**: This is the reality that can be experienced and observed in our everyday lives. If I were to throw a ball, I would be able to see the ball fly and eventually be pulled to the ground.
- **The Actual**: This is defined by events and phenomena, and since we employ a realist philosophy these events and phenomena occur unaffected by our ability to observe them. If a tree falls in the woods and no one sees it, the event will be no less real in its consequences. To the empirical realists the above constitute a comprehensive view of reality, however critical realists employ a third level of understanding.

- **The Submerged:** This is the underlying structures, causal mechanisms, and tendencies that drive the occurrence of the observable reality. These structures are highly complex and it is not only the existence, but also the interplay of these underlying mechanisms that shape reality. This allows for a more dynamic view of reality, where changes in underlying structures could create an outcome that diverges from the expected.

In order to engage in the process of knowledge creation it is necessary to uncover these layers. This is important when trying to understand the construction of the underlying causal mechanisms shaping reality at the surface. In terms of the ability to create generalizations around these mechanisms, we can only deduct tendencies of underlying mechanism. As a consequence, no laws or generalizations can be used to predict future events, due to the contingent character of these events (Benton & Craib, 2011; Buch-Hansen & Nielsen, 2005: 26-27). Thereby we are not attempting to predict consequences, but instead to address underlying layers explaining the functionalism of the causal mechanisms driving the emergence and design of the AIIB.

The CR perspective stresses a relational approach, meaning that pre-existing structures define the playing field for new structures to emerge. In this sense historic events do not define future events, but they affect the future outcomes by altering the plausibility of certain causal mechanisms. Furthermore, pre-existing structures and discourses creates the conditions and terms on which various mechanisms can interplay. Societal structures are deeply embedded in culture and norms, which is the pre-condition for the behaviour of actors within a system. In order to uncover the underlying mechanisms and structures described above, the CR perspective call for a pluralist methodology. This allows the researcher to mix a variety of theories and methods that is considered most beneficial in order to answer the research question (Buch-Hansen & Nielsen, 2005). This is further explained by the use of eclecticism described below.

Summary

Ontology	The world exists largely independent of our understanding of it. Reality is stratified and is created through the interplay of underlying mechanisms (some of these being dependent on socially constructed realities).
Epistemology	In order to create knowledge one must uncover the underlying mechanisms contributing to the formation of the observable reality. This comes

	with an acceptance of the importance of historical and situational structures affecting the event studied.
Methodology	The application of a retroductive approach to understand mechanisms that explain our experiences is an attempt to confirm or deny their existence. This underwrites a pluralist view of research methods.

(Buch-Hansen & Nielsen, 2005; Mingers, 2006: 31)

Eclecticism

CR allows for a pluralist methodology and since the aim of this thesis is to establish a holistic understanding of the case, it is necessary to employ thoughts from various academic disciplines. Eclecticism is an approach empowering the researcher to combine theory and research methods from a variety of traditional fields. Rudra Sil and Peter J. Katzenstein (2010) provide three main criteria for defining the eclectic approach.

Firstly, the framework allows the researcher to take a pragmatic approach, manifested in the exploration of theoretical arguments that fall outside the scope of traditional fields. In this thesis we will draw on theories originating from economics, political science, and behavioural science. The purpose of interdisciplinarity is to uncover the interplay between the various mechanisms in the global system, and an attempt to analyse various layers.

Secondly, eclecticism allows the researcher to practice a wider scope than traditional research methods. In order to incorporate real world “messiness” into the study a core aim of the thesis is to disentangle the complexity of the case. Through incorporation of economic, political, and behavioural implications we examine a broad spectrum, thereby not merely creating knowledge about the case but also addressing the broader field of development finance.

Thirdly, by examining a highly complex case the researcher’s analysis captures the interactions of multiple mechanisms at play – in this case in international development finance. Eclecticism allows us as researchers to combine ideas from different research paradigms to uncover a broader connection between the mechanisms that creates the stratification of reality. Alfred Hirschman framed the effectiveness of analytical eclecticism in the following quote:

> *"Ordinarily, social scientists are happy enough when they have gotten hold of one paradigm or line of causation. As a result, their guesses are often farther off the mark than those of experienced politicians… Likely to take a variety of forces into account"* (Sil & Katzenstein, 2010: 5).

In order for this approach to be successful it is extremely important to be cautious in the understanding and application of different methods. The careless application of theories will deteriorate the study and make it irrelevant. The next section will address some of the criticism aimed at CR and offer some considerations of specific pitfalls for this thesis.

2.2 Placing the Thesis within the Critical Realist Framework

One of the core strength of CR is the ability to move beyond the traditional dualisms in order to provide a more pragmatic and case specific approach to knowledge creation (Buch-Hansen & Nielsen, 2005). However, this strength can quickly turn into a weakness, if the researcher does not successfully clarify a philosophical stance on dualisms dividing the traditional paradigms. The realist-idealist and individualist-structuralist dualisms have been grounds for discussion. CR has received criticism for being vague and providing an insufficient argument for breaching certain areas of traditional practices (ibid). The aim of this section is to clarify our stance and approach to traditional debates on knowledge creation. Our framework builds on the ideas outlined above, however, in order to avoid unintended vagueness, we find it necessary to anticipate and specify our approach to potential grey-areas.

Realism vs. Idealism

It is important to understand that in critical realisms reality exists by itself and is not dependent on our acceptance. The mechanisms shaping reality constitutes both physical laws and social interaction. Physical laws are unaffected by our perception of them, while social interaction is highly determined by what is understood and perceived by the participating actors. Thereby, CR introduces some degree of social perception within its framework (Lawson, 1997). This fuels the complex argument that reality in its existence is independent of any individual perception. Yet, the mechanisms leading to the creation of future realities are to some extent dependent on the perceptions of individual actors participating in the central processes. This makes the effect of certain mechanisms dependent on the social context. In this sense it becomes interesting for scholars of social science to understand the underlying mechanisms of social interaction.

Structuralism vs. Individualism

A key question in the philosophy of social science is whether the individual is capable of taking actions unaffected by societal structures, or whether these structures dictate the actions of the individuals (Lawson, 1997). CR does not fully sympathise with either standpoint, as it is acknowledged that both contributes to the underlying mechanisms. According to critical realist's actors are biased by external structures (background and current situation), but structures does not impair independent action by the actor. This is an interesting question within development finance, because this field includes a large number of professions come from vastly different structural settings. However, there seems to be common ground around the need for increase infrastructure financing in developing countries. This thesis will attempt to uncover the barriers and the structures needed to create increasingly aligned incentives. Therefore, it is necessary to engage in the study of both structural and individual pressures in order to understand their interplay, and how they affect the outcome of key decisions. In order to engage in this exercise, we will employ an analytical framework introduced in great detail below.

2.3 Research Design - a Case Study

"What counts as a case can be as flexible as the researcher's definition of the subject" (Odell, 2001).

We have chosen the emergence of the Asian Infrastructure Investment Bank (AIIB) as our empirical subject of analysis. In particular, we are interested in understanding the reasons and motivations behind its emergence. We know that proof is hard to come by in social science, as no "hard" theory can be applied, but learning something is definitely possible (Flyvbjerg, 2006). Therefore, an in-depth analysis of a case can provide us with valuable insights that we would not have reached without such an approach. A case study is neither limited to reporting the facts or to provide an intuitive understanding of an event or phenomenon. As we are trying to answer *why* and *how* the AIIB has emerged, the case study research design is particularly well-suited (Yin, 2003). Furthermore, the disciplined case study preserves and reports more information about the specific case than a statistical study covering the same case (Odell, 2001: 171).

Specifically, we are conducting a *disciplined interpretive case study*. By applying an existing theory to a new event or phenomenon, the disciplined interpretive case study seeks to explain and reveal new knowledge about the case at hand. As Odell argues, the more explicit and systematic the use of theoretical concepts, the more powerful the application – this is what we hope to achieve by our two-staged analysis (see below). Although it is not necessarily the intention to test a theory, the case study helps us to understand how one or more known theories can be extended to account for the case (Odell, 2001: 163). This is what can create a broader interest from communities not directly interested in the case - here the AIIB. Furthermore, when the researcher pursues a disciplined application of theories, these naturally become more focused than might have been the case in other research designs (Eckstein, 1975: 103; in Odell, 2001: 163).

Another advantage with this type of case study is the high attention to detail in regard to concrete aspects of the case, something that the quantitative large-n methods cannot do the same way. Statistical methods only allow us to see a limited piece of the case, which have been subject to standardized indicators. Most importantly to state here is the risk of omitted variable bias when using these methods (Odell, 2001: 1970). According to Odell, these methods also tend to bias theory away from processes and towards structures. We are not saying that structures should be disregarded, but a sole focus on them is unable to explain much of the variation within them, as processes are essential for our understanding. When structures and institutions change, case studies provide us with the best knowledge of how those changes happened (ibid.).

As most cases can be subject to more than one interpretation, our case study method is vulnerable to selective reconstruction of aspects relating to the case which are in line with a prescribed theory, e.g. neglecting inconsistencies or evidence in favor of another theory (Odell, 2001: 164). By being aware of this potential weakness, we have created a theoretical model incorporating multiple and competing theoretical perspectives and apply it to our case in a way that makes a disciplined and transparent approach possible. The three different New Institutionalism perspectives will be used to answer the first part of our research question by analyzing the empirical data collected through our research process. Susan Strange's theoretical framework has been used to set the boundaries and focus of the second stage of our analysis and answer *who will benefit?*. Finally, by having different phases of research we have tried to increase the possibilities of asking a genuinely interesting research question and conduct more insightful and useful research.

2.4 Qualitative research – data collection and research process

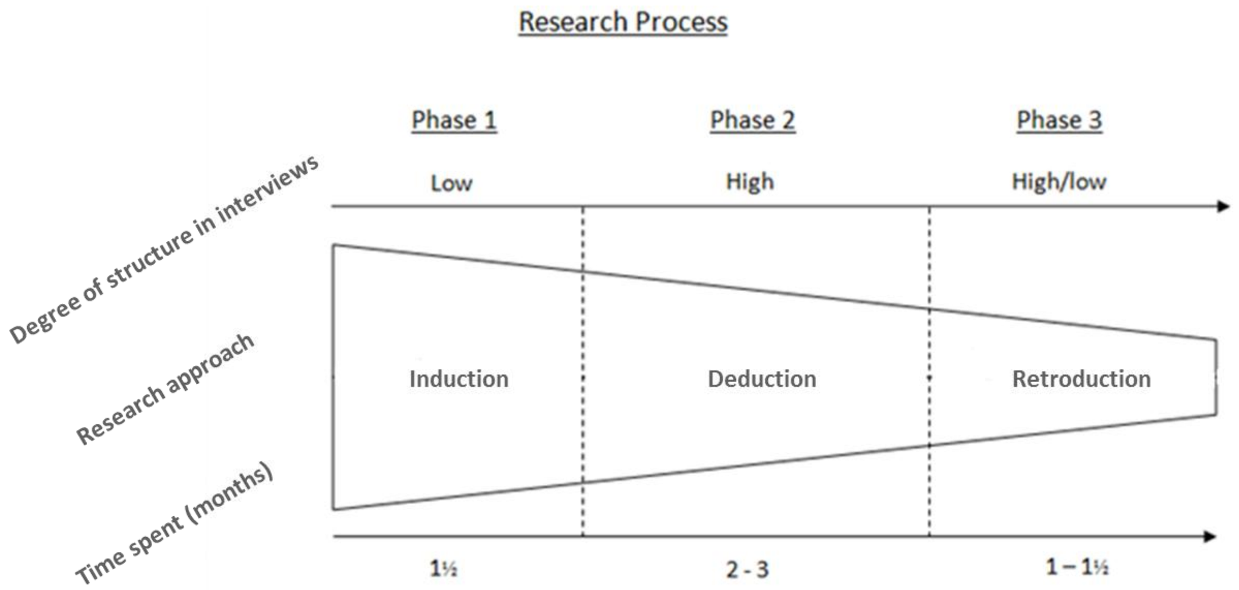
Aside from the information collected through desktop research, all of our data comes from qualitative interviews. It is therefore appropriate to lay out our research and thought process in this regard, as well as the methodological considerations that have guided our empirical data collection.

That being said, let’s start with some more general methodological considerations regarding qualitative research. As briefly touched upon in the previous section, quantitative research is from a positivist point of view seen as completely bias-free in regard to the influences caused by researcher bias (Yu, 2003). It’s the opposite in the case of qualitative research, where the researcher can be seen as the main instrument when it comes to collection, analysis, and interpretation of data (Onwuegbuzie, Leech, & Collins, 2008: 3). Being the main instrument, the researcher becomes very susceptible to biases, which we will discuss later in this section.

Scholars within the qualitative research discipline have recently argued for a serious rethinking of terms such as validity, generalizability, and reliability, as many other disciplines have already re-theorized these (Denzin & Lincoln, 2005). According to these scholars, this makes qualitative research faced with a crisis of legitimation, representation, and praxis, because it has to answer how it is to be evaluated in the contemporary moment. This basically challenges its ability to extract meaning from data (Onwuegbuzie et al., 2008: 3). To force ourselves as researchers to more awareness around these challenges, we have created a systematic research process.

Figure 1 illustrates the research process of this thesis. Worth noting is our awareness of different phases and therefore different kinds of advantages and disadvantages in each phase. As our case is a recent phenomenon and has a high level of complexity (as acknowledged in both the academic and professional communities associated with MDBs) and furthermore, given our initial lack of in-depth knowledge as researchers, we found it necessary to design a three-phase research process that included inductive, deductive, and retroductive phases. We chose a semi-structured interview technique (Kvale, 2008) to create three different basic interview guides one for each of the communities interviewed. The interview guides were updated to have varying degrees of structure, depending on which phase of research we were in. As we have primarily been interviewing respondents from three different communities; private sector, academia, and policy it was seen as the most appropriate way to collect data.

Figure 1



Phase 1 was characterized by an inductive approach to the research topic. This gave us the opportunity to explore different avenues and limit the bias, we as researchers, would have imposed on our respondents if we had let theory-driven questions take precedence, as we did in the deductive *Phase 2*. Before entering *phase 2*, we were faced with an essential methodological challenge – the challenge of assessing our own bias in and from *phase 1*.

Let's direct our attention for a while to what Matthew B. Miles and A. Michael Huberman (1994) very influentially have identified as the two fundamental sources of researcher bias. First, the effect of the researcher on the respondent, called Bias A, and secondly, the effect of the respondent on the researcher, referred to as Bias B (ibid.). We assess Bias A to be limited in most of our interviews, due to the fact that we presented ourselves as the master students we are. Nevertheless, it is worth stressing that the interviews conducted with high level respondents approached at the "Addis Ababa Financing for Development Follow-up Conference", may have been affected by the member state status (Denmark) we had as a consequence of access to the forum[1]. At the other end, we find Bias B that leads the researchers to go *native* - becoming a part of the research. As master's students we are intrinsically a lot more vulnerable to this kind of bias. A common critique directed at qualitative research is the lack critical reflections with reference to Miles and Huberman's (1994) Bias A and

[1] See appendix X for more details

B. What we strive to be particularly aware of is the role of these biases in the general research process, and in how it inevitably affects our findings and interpretations.

In acceptance of this challenge, *debriefing* as a means to limit and at best prevent us from drawing flawed conclusions, has been a crucial tool in the methodological toolbox applied throughout our research process (Onwuegbuzie et al., 2008: 3). Our point of departure was Onwuegbuzie et al.'s Miles and Huberman inspired framework for debriefing (Onwuegbuzie et al., 2008: 7). We used debriefing two-fold, both before entering new research phases and after interviews.

After each interview we wrote a separate debriefing and then compared and discussed our interpretations. This was particularly important after those interviews were we couldn't record due to confidentiality. We discovered as the research process progressed that we interpreted more and more the same findings from interviews. We see this as a natural consequence of a shared learning curve, but it also made us reflect more about which kind of respondents we would need to interview to test whether our interpretations were solid or too biased.

Being able to critically reflect on your own role as a researcher in a more systematic manner has the potential to improve the legitimization of our interview findings, and thereby mitigate the crises of legitimization and praxis in qualitative research (Denzin & Lincoln, 2005).

3. Background Information

The purpose of the following section is to give an overview of the role and operations of MDBs, and an introduction to the historic emergence of the World Bank. The World Bank has been central in defining the institutional trajectory of MDBs. Moreover, there will be a review of the Chinese approach to development and background for the new Sino-centric institutions[2]. This section is not intended to provide an exhaustive overview of international development, but instead provide the reader with an understanding of events relevant to our analysis. Therefore, the following merely seeks to provide a selective overview and understanding of the background and current situation. This section will be structured as follows; firstly, a brief review of the role and operational capacity of MDBs. Secondly, a historic explanation of the World Bank and a brief overview of the organizational structure and voting system and thirdly, a section on Sino-centric institutions.

[2] Referring to alternative financial development institutions created by, or partly by, China

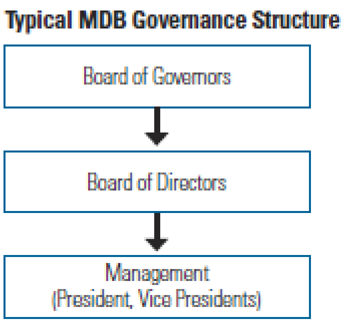
3.1 The Role and Operations of MDBs

An Introduction to MDBs

All MDBs share a common purpose, which is providing finance where other sources of finance are unavailable. In order to solve this task they also share similarities in the way they operate and their governance structures. This does not imply that all MDBs are completely similar, but essential features are replicated in most institutions.

An MDB is owned by its member countries and to become a member a country has to subscribe capital to the institution. The formula calculating the degree of voting power as a function of allocated capital is different among MDBs, but voting power is always connected to capital (Bob et al., 2015). It is important to note that a membership does not restrain a country from simultaneously being a borrower. This means there is not necessarily a distinction between borrowing countries and member countries. An MDB is typically governed through the following structure:

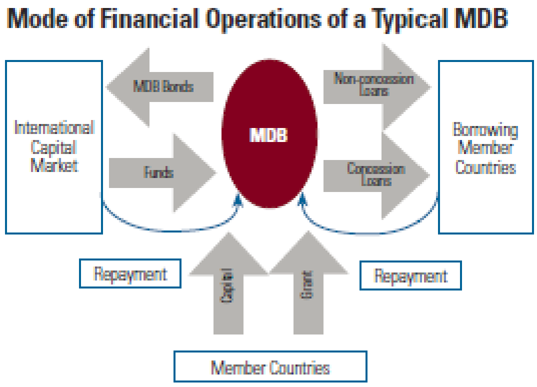
Figure 2



Source: Bob et al., 2015

The Board of Governors is the highest decision-making body, and is usually consisting of Finance Ministers from member countries or other high level officials. The Board of Directors (BoD) is the day-to-day decision making body. It is staffed by officials appointed by member states according to their voting power. MDBs can apply a resident or a non-resident BoD model. The majority of MDBs applies the resident model, however in the interest of increasing operational speed some MDBs have installed the non-resident model of BoDs. Such a constellation increases the decision making power of the management team, which is less political, and therefore often more effective in decision making. The management team is not politically appointed, and is therefore ideally not more accountable to any particular stakeholder.

Figure 3



Source: Bob et al., 2015

As the figure indicates, MDBs are capitalized by the member countries. MDBs also access capital from the financial markets through issuing bonds. This is the case for the self-sustaining type of MDBs. This type of institution gives mainly non-concessional loans, as they also answer to market stakeholders demanding a return on their bonds. This constellation is to avoid that member states will have to re-capitalize the bank. A bank giving concessional leans (IDA) is financed by grants from member countries. These banks do not have the capability to access finance in the markets, as their operational mandate is closely resembled to development aid. Therefore, this type of banks will have to be replenished by member countries to continue operations.

The Role of MDBs

To define the role of a *MDB* is an interesting and difficult task. The preferred role of a MDB depends on one's perception of effective development practices. MDBs, as other International Organizations (IO), emerge from high level negotiations, which tend to produce a degree of vagueness in the organizational mandates.

> *"(…) the organizational mandate of IOs is uniquely ambiguous, resulting from complex international negotiations that necessitate a healthy degree of vagueness to reach a final agreement among competing interests."* (Babb, 2003).

The general perception of the role of MDBs is to contribute to mitigate market failures and enable necessary financial flows to areas and sectors were traditional markets are unable to provide finance (Mistry, 2005). From scanning the literature, the role of a development bank can be divided into three major areas:

- **Funding and Finance:** Providing direct finance through loans and grants or enabling financial flows through guarantees.
- **Project Assistance:** Providing project assistance and contributing with project specific knowledge.
- **Institutional Capacity Building:** Contributing to institution building and political/systemic transformation in the borrowing country.

It is important to note that not all MDBs perform all tasks, but examples of varying degree of MDB participation in these key areas can be found throughout the history of MDBs. The World Bank is a pinnacle case, as it has experience and the internal capabilities to perform all of the tasks above. MDBs are largely dependent on their ability to adapt to external pressures and adapting adequately to turbulent changes in the external environment is an ongoing challenge for MDBs (Vestergaard, 2011; Mistry, 1995).

3.1.1 Funding and Finance

The common denominator of all MDBs is to provide finance with the purpose of promoting development. The financial input is given through grants or loans, which can be either traditional interest paying loans (Hard loans) or concessional loans with no interest (Soft Loans) (Mistry, 1995). Providing guarantees enables other types of finance to access an area, which initially had an unacceptable risk profile. The World Bank provides us with a good example of this structure, where the International Bank for Reconstruction and Development (IBRD) is offering hard loans, and the International Development Agency (IDA) offers soft loans (IDA, 2016). Other MDBs have similar types of separation such as, the Inter-American Development Bank (IADB) (hard) and The Fund for Special Operations (soft). These institutions are separated on different balance sheets due to their funding structures.

An IDA type institution is dependent on contributions from member states, as such an institution is depended on capital replenishment in order to continue operations (Buiter & fries, 2001). On the contrary, the IBRD has the capabilities of funding itself cheaply in the markets through issuing bonds. It can access cheap finance because it operates according to sound financial principles, and receives capital contributions from investment grade rated governments. The MDBs are capitalized through a relatively small amount of paid-in capital, and much larger amount of callable capital (Mistry, 1995). The latter represents capital allocated by member countries, not actually paid-in, but capital that is possible to call upon to mitigate institutional risk in cases of significant losses. To this date callable capital has not been used, but yet provides a solid case for strong ratings. The types of bonds issued by MDB have increasingly become sophisticated with continuous innovation in the underlying products. Green Bonds serves as an example as bondholders can deliberately chose to finance climate related projects (Buiter & fries, 2001).

Embeddedness of MDBs in capital markets was not originally intended. It has arisen as a consequence of unwillingness to supply sufficient capital from member states. In order to be self-supporting institutions, MDBs have had to refrain from taking excessive risk and investing in non-revenue generating projects (Humphrey, 2015). This was seen in the case of IABD, which initially invested mostly in social infrastructure, but as dependence on financial markets grew a more conservative approach focused on revenue generating infrastructure has been taking precedence. This has underlined the importance of IDA-type institutions to have the ability to provide development assistance to the poorest developing countries. In the case of the World Bank, IDA has been a positive addition functioning like a risk valve. This has allowed the IBRD to let riskier projects be undertaken by IDA, which has allowed for a decrease of risk in the portfolio (Humphrey, 2015). To summarize, a central constraint on the operation of MDBs is the financing structure. The degree of autonomy is decreased as a result of dependence on the relationship with members and external finance providers.

3.1.2 Project Development Assistance

MDBs vary in their capabilities and engagement in project development. Contributing skills and expertise in the development process has obvious advantages. When moving into poorer developing countries internal project development capabilities is a necessity to navigate a scarcity of good projects. Moreover, participating in project development on a global scale can contribute to a deeper level of expertise that can enhance effectiveness of future projects. However, knowledge creation comes at the cost of increasing organizational size and flexibility. This has proven to increase the length of the development process, and creates free-riding incentives for domestic stakeholders. Lastly, providing finance and project development have caused occasional bad projects, due to a lack of critically accessing one’s own project development work (EIB Report, 1998).

3.1.3 Institutional Capacity Building

The multilateral shareholder structure of MDBs provides a unique platform to address institutional capacity building. The cross-country reform experience, political palatable nature, and their ability to provide a material incentive for a given agenda, provides a platform for addressing institutional change in borrowing countries (Babbs, 2009; Buiter & fries, 2001). The participation of MDBs in domestic institutional building can be seen as an attempt to align incentives of the bank and the borrower. This ideally increases the likelihood of repayment and contributes to a robust development of the borrowing country. When engaging in large scale projects in institutionally weak states, MDBs can be seen as having a platform and expertise to drive structural reforms (ERBD). Studies have shown that the success of the reform ventures is largely dependent on the domestic political situation and design within the country (Dollar & Svennson, 1998). Thus, conditional finance (finance dependent on political reforms) has been effective when applied in states with a political climate supportive of structural reforms. Three main indicators have been identified to drive the successful use of conditionality; firstly, it allows governments to publicly commit to the implementation of a given change. Secondly, it helps finance the implementation of reforms which consolidates political support. Thirdly, it can help stipulate a positive response from investors through taking the first steps in creating a positive track record, especially in cases of private involvement (Buiter & fries, 2001). However, the role of MDBs in the area of institution building has been vividly debated. This has been exemplified in the heated debate surrounding the promotion of a neo-liberal agenda. The neo-liberal agenda intended to reduce government intervention in borrowing countries, to create a foundation for economic growth driven by market forces. This was coined the Washington Consensus (Babbs, 2009) resembling the American influence in promoting the free-market as a foundation for growth. It has served as a guiding framework for transitional demands proposed by IOs – and still does to certain degree (Babbs, 2009). However, competing development paradigms are emerging as new actors enter the development space (see section on Sino-centric institutions).

The following section will provide a closer look at the historic development and constellation of the World Bank. It is useful for reader to understand how the World Bank has shaped the MDB community, as the historical context is necessary to grasp the analysis.

3.2 The Historical Development of MDBs

3.2.1 The World Bank

The International Bank for Reconstruction and Development (IBRD) can be deemed as the mother of modern MDBs. It was designed in 1944, before the end of World War II (WWII), at the renowned Bretton Woods gathering. Given the timing of the formation, the initial purpose of the bank was mainly to assist the reconstruction of a war torn Europe (Lindbaek, Pfeffermann, & Gregory, 1998). The intellectual founders of the bank were US Treasurer Harry Drexler White and John Maynard Keynes (World Bank, 2016a). The influence of Keynes was reflected in the design of the bank, as it had a clear resemblance to a Keynesian world view. In Keynes' view, the world should be dominated by large active governments who actively direct and regulate economic activity (Lindbaek et al., 1998). Private actors were not trusted to operate central industries such as steel, coal, electricity, railways, and health care. These industries were viewed to be far too important to be left to private control. Hence, the IBRD was designed to be intrinsically intergovernmental and could only lend to the private sector if the loans were supported by government guarantees (Goldman, 2005). Secretary treasurer Fred Vinson wrote at the time about IBRD and the IMF:

> *"They are cooperative enterprises of governments and their chief business is with governments (…). They should not become just two more financial institutions."* (Humphrey, 2015).

The latter part of the comments hinted at the initial entrepreneurial vision of the bank. That vision was to give guarantees for governments borrowing from private sources, but the early leaders chose to pursue direct lending. This practice meant that the funds contributed by governments in capitalizing the bank were insufficient. The bank was forced into the markets to issue bonds as a means of finance for its loans. The need to appeal to the private sector played a large role in appointing John J. McLoy as the first President, a lawyer with strong ties to the financial community. The former banker Robert Garner was appointed as the vice-president. They were joined by the US appointed Executive Director, Eugene Black, a former VP of Chase National Bank of New York. The focus of the early loans was on operational soundness rather than achieving a development impact. Such behavior was driven by a need to gain legitimacy in the financial markets (Humphrey, 2015; Goldman, 2005). Through the 1950'ies the bank continuously ramped up its activities investing primarily in revenue producing infrastructure such as seaports, highway systems, and power plants. Focus was on middle income countries and loans were only given to low income countries on a specific project basis, with a strong focus on financial performance (Humpreys, 2015; Goldman, 2005). From 1947 to 1961 only 30 percent ($1.7bn) of the loans was dedicated to poorer developing countries. More than half ($1bn) went to Pakistan and India, countries with a strong geopolitical interest for the U.S.. The focus on financial performance let the bank to gain a good reputation, and allowed access to finance from the U.S. and world markets. This came at the cost of rigid terms for the borrowing countries (Humphrey, 2015). An increase in the pressure to support the poorest countries resulted in the formation of the International Development Association (IDA) in 1960. This new institution was originally to be placed directly into the United Nations system, but the U.S. negotiated strongly to implement it as part of the World Bank, giving the U.S. veto power. The latter setup eventually became a reality, despite developing country dissatisfaction (Babbs, 2009). This institution was given the mandate to work as the concessional arm of IBRD. Thus, it was allowed to give loans with the purpose of aiding the poorest countries, and essentially gave concessional loans with no interest rate, very long repayment times, and long grace periods (World Bank, 2016b).

The bank in its new constellation now included the IDA, and expanded into other sectors such as education, social services, and agriculture. Under the presidency of Robert McNamara the bank shifted its focus to poverty reduction, and introduced new ways of evaluating performance of projects (Goldman, 2005). Development finance had become a large scale activity, to some degree fueled by macro political interests related to the Cold War.

The deteriorating economic conditions throughout the 1970'ies, largely driven by an inflationary financing of the Vietnam War and the oil crisis led to a large increase in developing country debt. This made the World Bank focus more on loans to aid debt service (Lindbaek, Pfeffermann & Gregory, 1998). The global economic struggles changed the focus from development to more domestically driven concerns in Western states, and skepticism of development finance started to spread. This led to an increased demand for policies pushing for more private sector engagement and the privatization of public enterprises (Babbs 2009). This was coined as the Washington Consensus by the English Economist John Williamson (1990).

More recently the bank has begun to increasingly incorporate the view of civil society institutions in the pursuit of increased legitimacy. Such practices have led to a strong focus on safeguard measures in the operation of the bank. Safeguards are essentially operational policies that aim to secure minimal damage to the local community, the environment, and other unintended externalities of projects (World Bank, 2016c). Safeguard measures are criticized for adding a large layer of bureaucracy that is hard to navigate for borrowing countries. This makes some borrowers tend to look elsewhere before applying for World Bank loans (ODI, interview material). The World Bank attempts to address these issues through operational reforms currently in progress. Debates about the role of MDBs are ongoing and given the eventful 2015[3], development finance is now more relevant than ever.

3.4 Current Challenges and Background of the Rise of Sino-centric Institutions

This section will address the evolution of China's involvement in global development practices. The section will commence with a review of domestic and international efforts in building effective development practices. Then proceed to address the national and international background for taking the lead in establishing new institutions. It is beyond the scope of this section to engage into a large degree of detail, as it intends to constitute the background for an understanding of China's approach to development.

3.4.1 The History of Chinese Development Finance

The foundational principles of Chinese development practices date back to three major events: Mao's five principles developed in 1953, the Bandung conference in 1955, and Zhou Enlai's eight principles presented in 1964 (Xu & Carey, 2015). The Chinese idea behind development finance and aid is equality and mutual benefits, combined with a vision of knowledge sharing and non-interference. Hence, encourage recipients to assume responsibility of creating their individual development pathway (ibid). China's method to developing knowledge and capabilities in this field has been shaped by what could be termed as a learning-by-doing approach (Bergsager, 2012; Brødsgaard, 2010). Lessons learned domestically have been applied internationally and vice versa. To illuminate this, we will turn to examine the evolution of Chinese development finance.

The death of Mao in 1976 was the beginning of a series of domestic changes. From 1978 to the early 1990ies China went through a continuous reform process (Brødsgaard, 2010). This process gradually opened the economy and carefully allowed foreign investment to spark economic growth.

[3] Addis Ababa, Sustainable Development Goals, and COP21

Interestingly, China followed a very different path of economic development than prescribed by the dominant neo-liberal paradigm of the 1980ies. The Chinese development path was characterized by government protection of central interest in strategically important sectors. Measures used for protection was not traditional anti-trade measures, but instead control was enforced through support and implicit control of major state owned enterprises (SOEs) and the use of policy banks (Bergsager, 2012). While it is beyond the scope of this thesis to address the pros and cons of China's domestic development strategy, two interesting events characterize the financing of the reform process.

Firstly, the reform process enjoyed support from roughly $9bn of resource backed loans from Japan (Xu & Carey, 2015). A resource backed loan is a financial structure, where the loan is repaid in resources, in this case oil exports to Japan (Downs, 2011). Through receiving these loans China gained knowledge of loan structures, which allowed for the use of resource backed loans issued through their own policy banks (See below). This was as a central piece of their own process of development financing, and this type of financing had the additional benefit that the contractual structures of these loans assisted Chinese SOEs to expand abroad. These loans created a mutual benefit through an exchange of energy for assistance in the development of key infrastructure. The recipients were mainly African and Latin American countries, and in many cases Chinese construction companies won contracts to build large infrastructure projects abroad (Downs, 2011). Western countries have been questioning the level of mutual benefits of this model, but there is little doubt that it has benefitted China in developing both financial and entrepreneurial skill in this field.

Secondly, the role of the policy banks has been central in developing financial capabilities that have contributed to elevating China's role domestically and internationally. China has three major policy banks; The Chinese Development Bank (CDB), The China ExIm Bank (ExIm Bank), and the Agriculture Development Bank (ADB). An example the role of policy banks in domestic development is the Local Government Financing Vehicles (LGFV) issued by the CDB. These vehicles allowed local governments to raise money outside of their balance sheets. The revenue for repaying the loans was raised through the sale of farmland to the ongoing urbanization process. The CDB financed the loans cheaply through issuing government backed bonds purchased by the Chinese commercial banks. This helped finance rapid development, however, in the early stages the policy banks suffered from a large number of non-performing loans. A process forcing the policy banks to refine their loan given processes was initiated (Downs, 2011). Below, we will briefly address the international endeavors of the CDB and the ExIm Bank, as their operations to a certain extent resemble that of an MDB.

The CDB and the ExIm Bank have had considerable experience giving loans abroad. They operate in a vacuum where market failure makes projects ineligible for finance through traditional markets. This means that they provide a mitigation function comparable with the mandate of MDBs. The scale of the operations is notable, as the CDB had $251bn outstanding foreign loans, and the foreign loan book of The ExIm Bank was $96bn at year end 2013 (Xu & Carey, 2015). To compare the outstanding loans of IBRD, it was $155bn and $127bn for the IDA at the same time. However, when counting the domestic loans, the CDB had $1.154bn and The ExIm Bank had $234bn, outstanding at year end 2013 (ibid). As shown, the total size of these institutions is considerably larger than the World Bank.

A large part of the policy banks loans are given to developing countries. The banks proved willing to fund projects in countries with considerable institutional and political risk such as, Angola, Venezuela, and Ethiopia (Downs, 2011). Many of these loans have been of the resource-backed type, and have served strategic foreign political interests for China. The current changes in oil prices provide potential issues, but the effect has not yet been addressed by official sources in China. These banks have not only provided entrepreneurial support to SOEs, but have also provided support for private companies in sectors such as, telecommunications, technology, and green power generation (Xu & Carey, 2015).

The terms of the loans given through these banks are not concessional, but operate with thin profit margins in order to maintain a self-sustainable operating profile. In some cases, the loans have succeeded in crowding in other types of finance (Bergsager, 2012; Downs, 2011). The use of these financial instruments has helped spur the entrepreneurial capabilities within China, and has proved important in driving continuous economic growth (Xu & Carey, 2015).

It is undeniable that the lessons learned through the operations of these banks have contributed to building sufficient capabilities needed to undertake a leading role in building multilateral organizations. It is not within the scope of this paper to assess the operations of the policy banks in further detail, and a deliberately choice have been made to avoid the political controversies surrounding the operations of the banks.

3.4.2 The New Institutions at a Glance

This section will briefly touch on the two other major institutions recently emerged. It will not touch upon the AIIB, as it will be introduced in greater detail below in our case presentation. Firstly, we will provide a brief explanation of the BRICS bank, officially named the New Development Bank (NDB). This will be followed by an introduction of the Silk Road Fund, which is a heavily funded infrastructure fund operated by China.

At the sixth BRICS summit taking place on the 15th of July in Fortaleza, the countries signed the document sealing the creation of the New Development Bank (DIE, 2015). The bank will be capitalized with a $100bn, where an initial $50bn of subscribed capital will be contributed equally among the BRICS countries. In addition to the NDB, a BRICS Contingent Reserve Arrangement (CRA) of an additional $100bn will be created. China has committed to invest $41bn into this currency-swap institution (Reisen, 2015). The importance of China's role in NDB has been signified by the establishment of the headquarters in Shanghai. The NDB will be focused on long-term investments in infrastructure projects and sustainable development mainly in, but not restricted to, the BRICS countries. The NDB shares many similarities with the early investment project focus of the World Bank. The CRA is mandated with working to secure financial stability, through short-term support to relief payment pressures. This institution shares some similarities with the IMF. The presidency of the NDB will be a 5-year tenure rotating between the BRICS countries, where the first president will be an Indian citizen (Biswas, 2015). The voting structure is such that the BRICS will have an equal share of voting and their share can never subside below 55%. The NDB is open to contributions from other states, but given the rigid power structure and the investment focus it is unlikely that any developed countries intend to contribute. Smaller contributions from other developing countries are expected (ibid).

The Second major initiative, the Silk Road Fund, is driven solely by China and is structured as a fund with the intention to provide more connectivity in the region. China has announced a capital contribution of $40bn. This is funded partly by foreign currency reserves paid in through the

Chinese Investment Corporation, the CDB, and the ExIm Bank. The fund is intended to assume a structure similar to a PE investment fund, but the hold time of assets will be considerably longer, taking into account the developmental nature of the investments. The establishment of all three institutions almost simultaneously has the potential to change the power structure towards a bigger voice for developing countries within development finance (Biswas, 2015).

As noted above we have refrained from mentioning the AIIB in this section, as the following one will present this case.

3.5 Case presentation – the Asian Infrastructure Investment Bank (AIIB)

The following section will provide an introduction to our case, the AIIB. Starting with the words of AIIB itself, the purpose of the bank has been expressed this way:

"The AIIB will be a new multilateral development bank (MDB) designed to provide financial support for infrastructure development and regional connectivity in Asia. The purpose of the Bank is to: (i) foster sustainable economic development, create wealth and improve infrastructure connectivity in Asia by investing in infrastructure and other productive sectors; and (ii) promote regional cooperation and partnership in addressing development challenges by working in close collaboration with other multilateral and bilateral development institutions." (AIIB, 2016c).

Relevant aspects of this statement will be covered in the following section, consisting of timeline of establishment, membership and capital structure, governance, operations and financial instruments, and focus of investments.

Timeline of Establishment

On April 15th 2015, China's Finance Ministry revealed that 57 countries will comprise the Prospective Founding Members (PFMs) of the AIIB. But it all started in October 2013 when President Xi Jinping and Premier Li Keqiang announced the AIIB initiative. Then, a year after in October 2014, 22 countries signed the Memorandum of Understanding (MoU) to establish the AIIB headquartered from Beijing.

The first Chief Negotiators Meeting was held in November 2014, so the PFMs could start negotiating the Articles of Agreement (AoA). In the weeks up to the deadline for submitting a membership application, March 31st 2015, some of the big European countries signed up, initiated by the United Kingdom's decision to join. This meant that the final number of PFMs ended at 57, as mentioned in the beginning (AIIB, 2016a).

The AoA was then signed by all PFMs between June 29th and December 31st 2015. As Article 59 in the AoA states, the AoA can enter into force when at least ten countries have allocated a minimum of 50 percent of the AIIBs total capital subscriptions. The banks AoA entered into force December 25th 2015. At that time 17 PFM had allocated 50.1 percent (AIIB, 2016b). January 16th 2016 the AIIB was declared "open for business".

Membership and Capital Structure

The AIIB's members can be viewed as two groups consisting of 37 regional and 20 non-regional members. A regional member is defined according to the UN definition of being a country geographically located in Asia or Oceania (AIIB, 2016c). Regional members will contribute with 75% of the capital and the largest contributors are China, India, Russia, South Korea, Australia, Indonesia and Brazil. Of the non-regional members, European powers such as Germany, France, and the UK will be the main capital subscribers to the bank (The Interpreter, 2015).

Voting shares are calculated through a complex formula. The AoA do not state the breakdown of voting rights, although Chinese media have reported that China will have 26.06 percent (Global Times, 2015) while other sources have reported 29.78 percent (Lim & Mako, 2015: 2). According to article 28 in the AoA, a Super Majority of 2/3 of members representing 3/4 of votes is needed when it comes to major structural decisions made at the AIIB. To determine the total voting power of a member you have to count the Share Votes, Basic Votes, and when it makes sense the Founding Member Votes (ibid). All of this leads us to the conclusion that China will have an effective veto power in the AIIB as it looks for now.

According to Article 4 in the AoA, $100 billion of original authorized capital stock will be divided into $20billion of paid-in shares and $80 billion of callable shares. Allocation of shares among members is based on the relative share of the world economy (GDP). It should be noted that this is only indicative for the non-regional members (AIIB, 2016c). Furthermore, looking at the AoA you will discover unallocated shares totaling around $1.6 bn for regional members and $234 million for non-regional members – these shares are intended for additional members joining each category later on (ibid). Capital subscriptions are to be paid in 20 percent installments over five years. As a member you can pay in U.S. dollars or other convertible currency, which the AIIB can convert into U.S. dollars at any time. If you as a member are categorized as a less-developed country Special Provisions are made, as you can pay up to ten installments or pay up to 50 percent of the subscribed capital in your own currency (Lim & Mako, 2015; The Interpreter, 2015).

Governance

The overall governance structure of the AIIB can be viewed as a three-layer structure, which we have described the content of in the section below:

- **Board of Governors (BoG):** Highest governing body consisting of representatives from all member countries
- **Board of Directors (BoD):** The BoD will be elected by the BoG and will be responsible for management decisions. During the initial period of operation, the BoD will operate on a nonresidential basis, and then convene quarterly meetings to make decision on important policy areas. This is one of the essential differentiating aspects of the AIIB in regards to other MDBs. The BoD will consist of nine regional and three non-regional Directors.
- **Executive Management:** The executive management will be responsible for the day-to-day operations of the bank. Mr. Jin Liqun, a Chinese national, was appointed President and thereby also Chairman of the BoD, while 5 Vice-Presidents recently was appointed. These are the following:
    - Sir Danny Alexander (**United Kingdom**), Vice President, Corporate Secretary
    - Dr. Kyttack Hong (**South-Korea**), Vice President, Chief Risk Officer
    - Dr. D.J. Pandian (**India**), Vice President, Chief Investment Officer
    - Dr. Joachim von Amsberg (**Germany**), Vice President, Policy and Strategy

- Dr. Luky Eko Wuryanto (**Indonesia**), Vice President, Chief Administration Officer.[4]

(AIIB, 2016d)

Operations and Financial Instruments

The AIIB is created to provide financing for its members, governments, agencies, or enterprises, when they seek to invest in infrastructure projects. Throughout the first years of operations most investments will be made via co-financing with existing MDBs. Some of these existing institutions expressed an early interest in co-financing, for instance the EBRD with its President suggesting co-financed projects in 2016 (Reuters, 2015; Ashurst, 2015). The financing and instruments applied will take the form of sovereign direct loans, co-financing, investments in equity of institutions or enterprises, guarantees, and technical assistance (AIIB, 2016c; Griffith-Jonas, Xiaoyuan, and Spratt, 2016: 17). Infrastructure projects that are not guaranteed by sovereign credit will be financed through public-private partnerships (PPPs) or new innovative instruments. By sharing the risk and return with private capital, the AIIB hopes to attract the necessary capital from institutions such as sovereign wealth funds and pension funds. Investments with these actors will probably be administered through Special Funds (AIIB, 2016c).

Terms and conditions of financing, including interest rates and length of repayment, will be determined on a case by case basis. This will furthermore, be a consequence of AIIBs credit rating. Loans can be provided in the specific currency of the borrower, which may be very well-received by countries that has suffered from the currency fluctuations associated with their Renminbi loans from the Chinese ExIm Bank (The Interpreter, 2015). Regarding the procurement policy, is has been addressed as an open for all process, which means that even companies from non-members countries can participate in the proposals for goods and services procured in relation to AIIB-funded projects (AIIB, 2016c; Ashurst, 2015).

Initial Focus of Investments – Projects and Region

Much has been said about the AIIBs initial focus of investments – some more specific than other. The focus will for sure be on large scale infrastructure projects that could take the form of toll roads, power plants, seaports, and airports, which aligns with its mandate to promote economic development and regional cooperation (Ashurst, 2015). Through our interview with one of the lead

[4] See appendix for detailed resumes of management team

negotiators from the Danish Ministry of Foreign Affairs we learned that the overall sector focus of the AIIB would be water, energy, and transport.

The regional focus will be, as the name of the bank also indicates, Asia. Worth emphasizing though, is that if conditions permit the bank is allowed to explore investments in non-regional projects. This is interpreted to refer to developing signatory countries outside Asia (Ashurst, 2015; The Interpreter, 2015), or with the banks own words: *"(...) the Bank could be authorized to provide financing to recipients located outside the region that contributes to the economic development of the Asia region* (AIIB, 2016c). The last part of the sentence leaves some space for interpretation.

This regional focus is aligned with the "One Belt, One Road" initiative launched by the Chinese government in 2013. The Chinese expressed back then that the AIIB will be a main driver in achieving infrastructure development and integration in the region. The initiative is Chinas effort to create a link to Europe through Central and Western Asia, while the maritime version of the initiative is intended to connect China with all the South East Asian countries, Africa, and Europe (Ashurst, 2015).

Projected Project Pipeline

The AIIB have recently begun to announce the project proposals. The projects have yet to receive final approval but they are all expected to do so over the summer.

Country	Indonesia
Brief Description	The objective of the project is to improve access to urban infrastructure and services in Indonesian slums. The project would support an Indonesian governments program of urban slum infrastructure investments across 154 cities in the central and eastern parts of Indonesia. The project will consist of 20% Social Services, 20% Urban Transport, and 60% Solid Waste Management
Project Partner	The World Bank (50% of total project financing)
Project Size	Total project loan: U.S.$433 million, The AIIB contributes U.S. $216,5 million

(AIIB, 2016e)

Country	Bangladesh
Brief Description	The Project is designed to: (i) expand electricity coverage by providing 2.5 million new service connections in rural areas; and (ii) upgrade grid substations and convert overhead distribution lines into underground cables in northern Dhaka. The Project will supplement other development partner efforts by providing additional financial resources to connect more rural and urban consumers, further reduce distribution losses, and improve the quality and reliability of power supply in Bangladesh. The Project, upon completion, is expected to benefit about 12.5 million people in rural areas.
Project Partner	None
Project Size	U.S.262,29 millions

(AIIB, 2016e)

Country	Tajikistan
Brief Description	The project will increase the connectivity and mobility along the Tajikistan section of the Central Asia Regional Economic Cooperation Corridor 3 by rehabilitating the 5 km section of the road connecting Dushanbe to the border with Uzbekistan from the Avicenna Monument to the West Gate in Dushanbe.
Project Partner	European Bank for Reconstruction and Development (EBRD)
Project Size	Total project size: U.S. $105,9 millions actual split between EBRD and AIIB is currently unknown.

(AIIB, 2016e)

Country	Pakistan
Brief Description	The project will construct 64 km of a four-lane section of the motorway linking Shorkot to Khanewal in Punjab province of Pakistan. It will provide a faster, safer, and more cost-effective north-south route in support of the country’s economic and social development.
Project Partner	Asian development Bank (ADB) and the UK Department for

	International Development (DFID)
Project Size	Total: U.S.$173 millions actual split between ADB, AIIB and DFID is still unknown.

(AIIB, 2016e)

4. Theoretical Framework

The aim of this thesis is to analyze why the new Sino-centric development bank, The AIIB, has emerged and what implications this has for the development finance community. Moreover, it will be discussed if the AIIB could drive increased efficiency in the cooperation between private actors and MDBs. To answer this question, it is essential to ask ***why*** this new institution emerge and ***how*** the institutional design compares to already existing institutions. Furthermore, the question ***who benefits?*** is natural extension. Thus, the theoretical framework employed in this paper must provide a solid basis for addressing three major areas:

- The drivers of the emergence of major institutions within this domain
- The organizational design determining the capabilities of these institutions
- The framework for addressing who benefits from the emergence of new institutions.

The development finance field is a good case to illustrate the complexity of International Political Economy (IPE). It is an area where various actors interact to achieve multiple agendas. Hence, the interests of facilitating the economic development in developing countries are not the only agenda being pursued. It is a highly politicized field, which makes it an interesting case from an IPE perspective. Analyzing MDBs effectively calls for breaking down complexity to gain an understanding of the underlying mechanisms that dictate actions within the community.

We will be drawing on two major sources of theory, which will support the analysis of aforementioned ***why, how***, and ***who benefits***. Firstly, we will use New Institutionalism to explain the emergence and design (*the* ***why*** *and* ***how****).* This will be accompanied by the application of the IPE theory created by Susan Strange, the Strangeian School (Revell, 2006). This theory will be applied to the question ***who benefits*** from the emergence of the AIIB. These two theories and how they will be applied in this thesis will be explained in greater detail below.

This section will proceed as follows: Section 1 will provide a detailed account of New Institutionalism and how it is applicable to our case, the AIIB. Followed by section 2 introducing the theoretical approach coined the Strangeian School. Section 3 will be dealing with the interplay of these perspectives and their application to the study of the emergence and change of institutions in complex international political environments.

4.1 Theory Review – New Institutional Theory

Institutionalism

Defining the emergence of institutionalism is a difficult task, since there is little consensus of the first appearance of the approach in academia. The main reason for the lack of consensus is the broad foundation of institutionalism. The study of institutions has been undertaken across various disciplines, which has made it difficult to unanimously define the emergence of the theory (DiMaggio & Powell, 1991). A brief account of selected contributors to the development of institutionalism is offered below.

The early political economists, such as Karl Marx and Adam Smith, addressed the rules and structures of society. They can be seen to have contributed to the early establishment of the modern study of the role of institutions. Institutions can be defined as structured and observable, but can also be defined as a set of rules and cultural customs that guide social behavior. Here it is important to mention the work of Thorstein Veblen. His work took a Darwinist approach to economic sociology. Given the inspiration from Darwin, Veblen's work is sometimes referred to as Evolutionary Economics (Dugger, 1979). He is considered one of the first institutional economists since he introduced the idea of separating the influence of institutions and technology. This approach was coined as the Veblenian dichtonomy by his peers (Waller, 1982). Veblen acknowledged that institutions are created and designed by people, but simultaneously existing institutions play a role in shaping the ideas of the people. This perspective is both functionalist but yet acknowledges the structural pressures presented by institutions, resembling the term path-dependency (Dugger, 1979).

The idea of institutions being real and observable structures was key in creating the foundation for the formation of institutional economics. This theoretical view had strong ties to contemporary Rational Choice Institutionalism (see below). Yet, the view of institutions being observable structures was accompanied by scholars defining institutions to be more sociologically complex. In their view institutions had an impact beyond the observable structures. This has inspired numerous sociological studies of the effect of institutions. When discussing a sociological approach to institutionalism, it is necessary to mention the work of Max Weber - often viewed as the founding father of modern sociology (Hall, 2009). Weber emphasized the role of bureaucracies in society and how the process of bureaucratization created an "Iron Cage". In the Iron Cage the freedom to act was constrained within the defined "walls" of society. This empowered the bureaucracy with the institutional power to guide the actions within its domain. This thought is the foundation of the contemporary theory of institutional isomorphism (DiMaggion & Powell, 1983). Henceforth, the thoughts of Weber were of central importance to Parson's development of what was termed the structure of social action. This is basically the idea that social action is constrained by both cognitive and structural barriers within a society.

It is to be noted that the description offered of the works Weber and Veblen is a gross simplification and does not justify the depth of their scholarships. However, it will become apparent below that the ideas introduced by these classic scholars have provided a foundation, on which modern scholars have built what is now coined as New Institutionalism.

The Emergence of a New Institutionalism and the Tale of Three Institutionalisms

The New Institutionalism is not as "new" as the name suggests. It arose as a response to the rise of behavioral approaches emerging in the 1960ies and 1970ies (Hall, 2009). These approaches viewed institutions to be epiphenomenal and existing merely, as the sum of their individual properties (Dimaggio & Powell, 1991). The main motivation for New Institutionalism was to move institutions back into a central position in social science, and use the progress of existing theory, to create better explanations for the emergence, persistence, and change of institutions.

New institutionalism does not constitute a unified body of thought; it is rather a collection of approaches with different seminal perspectives on the main drivers of institutional activity. The major differences in academic activity can be boiled down to the application of a calculus or a cultural approach. These describe a general stance on the following questions: *How do actors Behave? What do institutions do? And Why do institutions persist over time?* (Hall & Taylor, 1996).

Table 1

	Calculus	Cultural
How do actors behave?	Humans behave based on strategic calculation by working to maximize utility in relation to a defined set of goals. The goals and preferences of an actor are given exogenously of the institution.	The cultural approach stresses that while human behavior is to be seen as purposive and rational, it is not fully strategic as it is bounded by the worldview of the individual. This defines individuals as satisfiers rather that utility

		maximizers and stresses that decision making is based on an interpretation rather than calculation.
What do institutions do?	Institutions affect behavior by providing actors with greater or lesser certainty about the future behavior of other actors. Thereby, institutions provide actors with intelligence on which to base strategic decision making with the goal of maximizing future utility.	Institutions provide moral and cognitive templates for interpretation of action. The individual is seen as deeply embedded in existing institutions. Institutions provide strategic information but simultaneously play a large role in shaping the identity and preferences of actors.
Why do institutions persist over time?	Institutions exist because they employ what could be described as a Nash equilibrium. Meaning that a change in institutional behavior will be damaging for actors within the institutional system. The more actors gain from transactions embodied by an institution the more robust the institution will be.	Institutions are persistent because they shape the decision that are made within the institutional realm. Thereby institutions are resistant to redesign because they structure the choices about potential reform.

The distinction between a cultural and calculus approach to the study of institutions is central in Hall & Taylor’s (1996) elegant description of the three main strands of institutionalism:

- Rational-Choice Institutionalism (RCI)
- Historical Institutionalism (HI)
- Sociological Institutionalism (SI)

A simplified distinction between the three could be made in their application of the calculus and cultural approach.

Figure 4

Rational Choice Institutionalists are consistently applying a calculus approach, which is closely connected with Institutional Economics and New Organizational Economics (Moe, 1984). Historical Institutionalists employ an eclectic approach allowing them to combine the approaches in a pragmatic way, where sociological institutionalist use the cultural approach (Hall & Taylor, 1996). The following sections will be dedicated to explain each strand in greater detail.

4.1.1 Rational Choice institutionalism (RCI)

The RCI strand of institutional studies was developed in the 1970ies, as a response to behavioral theoretical developments in the 1960ies and 70ies. This theoretical strand is, as indicated above, based in the calculus approach to the study of institutions. It draws heavily on New Organizational Economics in the sense that property rights, rent-seeking, and especially transaction costs are heavily emphasized as important aspects of understanding the behavior of institutions (Moe, 1984). Institutional behavior is seen to be strategic, and politics is seen to possess game theoretical characteristics. Hence, all actors seek to maximize utility given their expectations of the future moves of competing actors. In that sense, institutions are seen to exist in a competitive environment (Hall & Taylor, 1996).

Institutions exist in an attempt to reduce transaction costs for a set of actors (Williamson, 1975). Institutions are successful and persist, as long as they continuously serve the purpose of effectively reducing transaction costs. Peter North (1991) argued that institutions are more rigid due to the "cost of change". Thus, it is necessary to take the cost of changing institutions into account when evaluating the persistence of institutions. This means that the institutional existence is a product of a rational cost-benefit calculation driven by the potential benefit of institutional change vs. the cost of changing institutions.

RCI undertakes a deductive approach to study the performance of institutions. The contributions by RCI have led to a more precise conception of the relationship between institutions and behavior. This has led to developing a highly generalizable understanding of institutional behavior (Hall &

Taylor, 1996). RCI allows for a very elaborate analysis of the role that human intention plays in political outcomes, and provides the most elegant account of institutional emergence and persistence.

It has to be noted that RCI struggles to provide the same elegance in the explanation of institutional change and change in the institutional equilibria. Moreover, the generalizability is achieved through employing a simplified image of human motivation, and through overplaying the intentional behavior of central actors. The analysis is limited in the sense that the outcome is dependent on a definition of preferences that happens exogenously to the analysis and often requires some degree of assumptions. This means RCI underplays the importance of power structures, which is much more central to the analysis of Historical Institutionalists.

4.1.2 Historical Institutionalism (HI)

The HI perspective was developed simultaneously with RCI, but the two perspectives developed in relative isolation from each other. Early HI scholars borrowed from earlier theories of structural functionalism, rejecting traditional functionalism as an appropriate approach to understanding institutions (Hall, 2009). The eclectic epistemological stance employed by HI scholars allows for a "pick and choose" approach, which enables the incorporation of multiple influential factors of both structural and functional nature to the analysis (Hall & Taylor, 1996).

HI scholars generally describe political interaction, as a degree of conflict among rival groups over scarce resources, and institutions are both a result of the power struggle but simultaneously they determine the playing field (Hall, 2009). Thus, the HI perspective puts a large emphasis on power structures, and focus on examining the inequality that is seen to drive outcomes of institutional interaction. Institutions are seen to be the principal factor for generating outcomes in the political economy and focus is largely on the structuralism implicit in the institutions rather than their functionalities (Hall & Taylor,1996). HI takes a critical view of the state and does not consider the state a neutral broker in power struggles (Katzenstein, 1978; Evans, 1985). This resembles the thoughts of a Marxist approach to state interaction in society. Moreover, the HI perspective takes a temporal approach to institutional development, where historical events and existing structures play a large role in determining the future development of institutions. Thus, demonstrating that the concept of path-dependency is embedded in HI analysis. It is important to note that institutions are not solely seen as political constructions, but are also a product of other factors such as diffusion of ideas and socioeconomic development (Hall, 2009).

Induction is used as the guiding principle in knowledge creation, which constitute a significant difference from the RCI perspective. HI provides a strong basis for creating knowledge of the power structures within an institutional framework. Institutional change is explained through changes in the power structures. The incorporation of a multitude of structural and historical factors provide a strong narrative that produce a deeper more detailed account of interaction, compared to the simplified motivational structures employed in the RCI perspective (Hall, 2009). However, this more complex set of drivers, combined with the eclectic approach, has shown to limit generalizability. This has caused the lack of a clear causal chain to how institutions affect the behavior they are meant to govern (Hall & Taylor, 1996). It has led HI to be slower in producing systematic theories than other strands of institutionalism (Hall, 2009).

4.1.3 Sociological Institutionalism (SI)

The SI perspective emerged slightly later than the RCI and the HI. It set out to address the effect of socialization in the interaction of institutions. This perspective draws on the cultural epistemological approach that stresses the importance of culture in defining and accepting certain institutional designs (Hall & Taylor, 1996). It can to a large extend be seen, as a reaction to Weber's thought on the "Iron Cage" (Baehr, 2001) and scholars of this branch stress that institutions are not driven purely by rationality. Instead, cultural norms and subjective understandings of reality are of central importance (Dimaggio & Powell, 1983).

The SI perspective define institutions more broadly by also including symbol systems, such as cognitive scripts and moral templates, which contribute to create the *frames of meaning* (Hall & Taylor, 1996). Institutions are defined as the structures that enforce the ideas and norms that creates the cultural glue in society. The analytical approach of SI shares strong resemblance to social constructivism (ibid). According to SI, institutions emerge through an understanding of shared issues by the central actors. Institutions can be seen as primarily enabling structures enforcing the *logics of appropriateness*. Similarly, legitimacy and social appropriateness is central to the persistence of institutions. The importance of legitimacy means that even the most rational bureaucratic functions are explainable through cultural pressures and an aspiration to gain social appropriateness (DiMaggio & Powell, 1991). Following this logic, institutional change is seen to be a function of changes within central cultural processes within a society.

SI successfully breaks down the area between norms and institutions, and effectively explain behavior through cultural preferences and the quest for legitimacy, rather than a quest for achieving optimal economic efficiency (Hall, 2009). The SI analysis is limited in its insufficient attention to incentives and lack of recognition of deliberate action. Moreover, the importance of power structures in institutional interaction is underplayed (Hall 2009).

Table 2

	RCI	HI	SI
General	Employs a calculus frame of analysis. Draws on lessons from New Organisational economics. The core function of institutions is to administer property rights, rent-seeking and transaction costs.	Employs an eclectic frame of analysis. Takes a temporal approach to the creation of institutions and emphasise the role of path dependency in affecting change. It is very focused on power relations and institutional creation is seen as a result of power struggles. The state is not seen as a neutral broker in societal power struggles.	Employs a cultural frame of analysis. According to the Sociological perspective institutions are not emerging due to purely rational thinking but is guided by the cultural pressures determining how actors interpret the world around them. There is a strong focus on legitimacy and social appropriateness.
Definition of institutions	Institutions are seen as defined organisational structures, which seek to maximize the benefit for a set of actors.	Institutions are shaped through historical power structures by actors competing over limited resources.	Institutions are generally defined as the structures that institutionalise norms and values.
What causes institutions to persist?	Institutions persists as long as they provide a solution in which benefits of institutional change is less that the cost of change.	Institutions persist as a result of unchanged power structures and path dependency.	Institutions persists as long as they are coherent with the norms and values of the society as a whole.
What causes institutional change?	Institutional change happens when institutional equilibrium is disturbed.	Institutions change as a function of changes in power relations and within the possibilities for change determined by existing structure (path-dependency)	Institutions change as cultural pressures changes the societal requirements for achieving legitimacy.

4.1.4 A Collaboratory Approach: Issues and Benefits

This thesis will employ all three perspectives of new institutionalisms. The choice to do so is driven by the desire to contribute to a better understanding of how these theories could benefits from concepts applied within other disciplines. In order to do so, it is necessary to take an interdisciplinary approach to understand the institutional change presented by the AIIB. We acknowledge that such an exercise requires careful consideration, to avoid creating a universal theory possessing purely descriptive capabilities (Hall, 2010). To avoid this blunder, we have made a conscious choice to refrain from attempting to combine all three into one overarching theory. Instead we will perform an individual analysis applying each perspective in separation. We acknowledge that these three perspectives have the ability to create analytical synergies, potentially contributing to a deeper understanding with greater explanatory power. This will be described in greater detail in the section focusing on our analytical framework, but first we will turn to a discussion of the complimentary potential of these three theories.

This can be discussed in great length, but in order to avoid going into unnecessary detail, three main points will be discussed to establish the existence of strength and weaknesses across theories:

- Intentional Strategic Actions
- Path-Dependency,
- Institutional Ambiguity

Peter Hall (1996; 2009) has argued for an increase in collaboration across intuitionalisms, driven by the idea that each strand is successful in explaining parts of institutional behavior, while having limitations.

Intentional Strategic Action: The rational choice perspective provides a strong tool for examining the strategic characteristics of institutional interaction. The perception of actors as rational and calculated in assessing benefits of a given decision, is effective in creating a simplified understanding of the variety of agendas driving individual actions. Thus, this approach has proven to be a useful tool for understanding cases of institutional emergence. Understanding all actions as carefully calculated is underestimating the importance of socially constructed ambiguity and the lack of information. RCI have also been criticized for underplaying the importance of power and interdependency structures in assessing decisions. Scholars would agree that the establishment of institutions, as well as institutional change, is affected by the existing structures of influential bodies. This an area where RCI scholars could effectively learn from HI scholars. HI has a strong emphasis on the effect of power and existing structures, but in turn does not present the same clear explanatory power displayed by the RCI analysis (Hall, 2010).

Path-Dependency: Is a strong tool for understanding how existing institutional constellations affect the success of change related actions. It allows to embed institutions in the context and to address central power discrepancies in the analysis. This has been shown to have a large importance, by Hall & David Soskice’s (2001), in their study of the effects of the constellation of domestic economic regimes on institutional developments.

Institutional Ambiguity: Is often viewed to be underrepresented in both RCI and HI, but the SI approach have been successful in addressing the social construction regarding institutions and emphasizing the importance of perception and social legitimacy (Hall,2009). This aspect is to a certain extent incorporated by HI scholars, but would be immensely difficult to incorporate in RCI analysis as it is counterintuitive to this type of analysis. This emphasizes that each perspective has a certain explanatory power, but there is a potential to improve the theoretical foundations by cautiously incorporating ideas from other perspectives.

This has given rise to the idea of approaching institutionalism in a more interdisciplinary manner (Hall, 1996). Understanding the strengths and weaknesses of each theory in greater detail, can contribute to improving analytical strength. It needs to be noted that the view taken in this thesis is that a single theory combining the three strands will likely result in a theory that provide a purely descriptive analysis.

4.2 Theory Review- Susan Strange & Structural Power

Susan Strange is often referred to as one of the most influential scholars of International Political Economy (IPE). Her contributions have been vividly debated, both during and after her scholarship ended in 1998. This section is dedicated to illuminate her theoretical contributions and how they are relevant for this thesis.

The Origination of the Theoretical Thoughts of Susan Strange

The scholarship of Susan Strange is wide ranging, but for the purpose of this thesis focus will be on her approach to the study of structural change in IPE. At the time of her writings the traditional state-centric realist position had long been dominant in the study of International Relations (IR) (Sell, 2014). However, alternative positions were emerging and the field of IR appeared to be calling for new approaches to gain a deeper understanding of the changes arising (Revell, 2006). Economic globalization was increasing the participation in the international markets and financial interactions had reached new degrees of complexity. Thus, producing an increase in the economic interconnectedness of developed and developing countries (Leander, 2001).

The effect of technological progress generated new communication possibilities, increased globalization pressures, and the ease at which financial capital could relocate. International economic agenda setters pushed for increasing economic privatization and deregulation, which amplified the social power of private actors (Tooze & May, 2002). The distribution of power in this new structure could be argued to transcend the importance of states and contribute to a change in the dynamics of IR. This led to a greater role of private actors in theoretical considerations (Sell, 2014). Susan Strange emphasized the state-market nexus, where the political authorities and the economic market interact in order to create a given outcome. This indicates a dynamic relationship, a kind of continuous bargaining. In her view, the authority over a bargaining situation is not dependent on the actor being a state, but could also be private actors, international organizations, and NGOs. The outcome of the bargaining will reflect the power distribution between the state and the market. Inspired by these developments, Strange saw it as inadequate to focus on states as the main actor, which increased her focus on private actors (May, 1996).

She strived to make contributions that were relevant beyond the academic world, a focus that led her to take a pragmatic approach to the use of the –isms (realism, functionalism etc.). Hence, allowing her a sense of freedom to perform analyzes designed to have sufficient explanatory power beyond the field of academics. This meant undertaking a pluralist ontology driven by a desire to answer the pragmatic question of **w*ho benefits?*** (Sell, 2014).

Thoughts on the Study of Power

According to Strange, an understanding of where the power lies and how power distribution affect bargaining positions is central to any analysis of IPE.

> *"It is impossible to arrive at the end result, the ultimate goal of study and analysis of study and analysis of the international political economy without giving explicit or implicit answers to these fundamental questions about how power has been used to shape the political economy and the way in which it distributes costs and benefits, risks and opportunities to social groups, enterprises and organizations within the system"* (Strange, 1976: 22).

To grasp the underlying determinants of the understanding of power distributions it is necessary to undertake a brief journey through essential arguments of past scholars. These scholars have contributed to developing the understanding of power. We commence from the definition of power, as being the production of intended effects. Adding to this understanding Russell argued that in the absence of institutions guiding an interaction, power is likely to reside with the actor possessing the largest desire to obtain it (Russell, 1938: 10). Peter Blau (1977), contributed with three major points expanding on Russell's original argument.

Firstly, he added a behavioral aspect to the concept of power by arguing that power lie with the person who has the ability to impose his will on another - will being defined as the desire for an intended effect. Secondly, he contributed to distinguish power from force by arguing that there is an element of voluntarism in the application of power. An actor is faced with a choice of accepting the punishment related to non-compliance, distinguishing power from force where the element of choice is absent (May, 1996). Thirdly, he defines power as an asymmetrical relation. Steven Lukes (2005) moved on to provide three dimensions of power, which provide a useful transition to the ideas of Strange. His one-dimensional view is largely similar to what is offered by scholars discussed above. In this view power is what determines why one view precedes over another. In his two-dimensional view he includes the possibilities of prohibiting decisions from being taken. Thus, an actor with power within a relationship enjoys the ability to postpone decisions possibly indefinitely (May, 1996). The third-dimension is concerned with how power can keep certain issues out of the decision making process. In this view power is defined as the ability to set agendas, leading to a potential creation of latent conflicts. These conflicts are driven by differing interests between agenda setters and the agenda takers. The third dimension of power is very similar to Strange's definition of structural power, which is outlined in greater detail below. The agenda setting power dimension offers an interesting foundation for understanding power structures within development finance.

In order to understand the power structures, Strange advocates a separation of power into relational power and structural power. **Relational power** is defined, as the capacity of A to get B to perform an action that B would otherwise not have performed. **Structural power** is defined as the power to shape and determine the structures that define the arena for interaction, and the ability to directly or indirectly affect the agendas upon which decisions are taken (Revell, 2006: 24; Germain, 2014). It is important to note that structural power is dependent on a degree of legitimacy, where relational power can occur unheeded of the existence of the legitimacy of the action (Germain, 2014). Legitimacy being defined as the recognition of the actors, the methods or structural arrangements that exercise or facilitate power as corresponding to the mandate that has been entrusted on the given entity. Different scholars acknowledge the central drivers of legitimacy as being transparency, openness, neutrality, substantive quality, and consistency (ibid). However, the perception of legitimacy is also deeply embedded in the structural power configurations, where an actor can achieve legitimacy through skewed interdependency in relations (Strange, 1998). In Strange's view changes in structural power are more persistent than changes in relational power, as this type of change goes beyond situational decision making. Hence, structural power constellations serve as foundations for future systemic constellations (Tooze & May, 2002).

A brief illustrative example of structural power in international finance is the voting system in the IMF. This system gives western economies a higher proportion of votes than is justified by their comparative share of global GDP (Vestergaard & Wade, 2014). This can be seen to have direct impact on leading the decision making process towards a given set of values. The process is arguably affected indirectly and directly by the ideological preferences associated with countries benefiting from structural power. It could be seen to create an asymmetric dependency relationship, where Western "have" states exercise power through international organizations by determining the playing field for the development of "have-not" developing states (Germain, 2014). Similarly, Strange see domestic political agendas and social arrangements within powerful states to be central in determining the agenda of international decision making (May, 1996).

According to Strange the price of non-participation in the world economy has become exceedingly high, which results in relationships characterized by strong interdependencies (Leander, 2001).

> *"Opting out of the world market economy is no longer an option. That is what dependency means today"* (Strange, 1994: 215).

Comprehending the underlying mechanisms of these relationships is central to grasp the power structures at play between developed and developing countries. Moreover, the international financial markets have become a central arena in the struggles to satisfy both public and private interests. The recent financial crisis is a telling example of the interdependency and the significance of financial markets. The crisis was driven by a financial system that had gotten out of control, which Susan Strange had identified as a system allowing behavior comparable to gambling in her books Casino Capitalism (1986) and Mad Money (1998).

Strange emphasize three main dimensions of the analysis of structural power. Firstly, she emphasizes the state-market nexus. This refers to the analysis of how the political authority and the financial market interact to create a given outcome. It is an indication of a dynamic relationship, a kind of continuous bargaining where the authority over a bargaining situation is reflected in the outcome of the game (May, 1996).

Secondly, according to Strange it is important to analyze the underlying values driving these bargains. Strange defines the basic human values provided through social organization as being, wealth, security, freedom, and justice (May, 1996). It is important to understand how these values are prioritized by the actors in the bargaining process, as it will reveal what values are sacrificed to promote other. This follows the thought that no bargaining process is value neutral - an agenda is always present.

Thirdly, the allocation of risk is seen as an important consideration in understanding the power structures. It is necessary to understanding how states and markets creates risks and how these risks are mitigated or converted into costs. Risk is perceived to be present both before and after the bargaining, but are likely to have significantly changed through this process. In Strange's later work the analysis of risk becomes more submerged and takes a more implicit character. But May (1996) argues that while it may not be as visible, it is still very present as an underlying mechanism of the analysis.

Strange was critical to the traditional functionalist approach to the study of institutions. This approach analyze institutions through their functionality, and she saw this type of analysis as overly simplistic and lacking the influence of power structures (Sell, 2014; Germain, 2014). However, it is impossible to deny that the MDBs are important market making institutions in development finance (Bob et al., 2015). They also constitute a potential gateway for increased private involvement in a space that has traditionally been controlled by public actors. Therefore, the study of these institutions and their embeddedness in the existing market and power structures, is central to understand the structural implications of the emergence of the AIIB.

4.2.1 The Strangeian Four Pillars

The Strangeian approach (Revell, 2006) provides an analytical recipe to the study of structural change. This approach takes a holistic perspective and employs a pluralistic methodology. It is arguing for increasing interdisciplinary thinking between international economics and international relations. Thus, it is seen it to be insufficient to limit the analysis to the structures of production and trade, as is custom in IPE (Germain, 2014). In order to undertake this type of analysis, the Strangeian approach use a framework based on the study of four main pillars:

Table 3

Money & Finance	This pillar is concerned with the governing of the market structure and the availability of credit. Important here is the interplay between private and public finance. The ability to supply credit is dependent upon

	gaining the confidence of the market, which also determines power. Power in this structure is held by actors who are central in the process of setting the terms of the market, and with the ability to drive structural change through enforcing own interests through innovative solutions. Moreover, the actors who are central within determining the structures of dependency holds the power.
Knowledge	This pillar comprises the relations under which knowledge is produced, stored, communicated, and how the use of knowledge affects the bargaining process. It includes what is believed and generally accepted as understood. There has been debates about the understanding of knowledge and the interplay and separation between beliefs and information. Actors with power in the knowledge structure are those who are in a position to determine what knowledge should be produced, and determines what is considered legitimate.
Production	This pillar determines how wealth is produced under what terms, and especially who decides the terms of production processes. Changes in production structures can be seen to alter the very nature of a given state. The power here lies with the actors with the ability to determine what is produced and what terms apply to the production and procurement process.
Security	This pillar concerns the supply of security. Security is defined as the protection of people from common dangers. It could be both climate change, war, or economic collapse. The power in this structure lies within the ability to determine the agenda and the arena in which security concerns are tackled. Security structures are often seen to be affected by pressures from the three other structures.

These four pillars are seen to be better equipped to tackle the increasing complexity of the international system. It is important to acknowledge that all four pillars will *not* have a similar explanatory weight in all cases (Revell, 2006). Thus, the Money and Finance pillar could have more explanatory power in one case, where the knowledge pillar is less influential and vice versa. Hence, the purpose of four pillars can be viewed as a way to limit complexity and gain sufficient analytical depth. Central factors can be separated and understood disconnected from the structure as a whole (ibid).

The inclusion of knowledge has been vividly debated, as this has been deemed a controversial theoretical addition. The debate has taken various directions, but most prominently it has been seen as epistemologically problematic to include knowledge as a central analytical pillar. The problem is two-fold, firstly, the definition of knowledge is deemed as problematic since beliefs and information is seen to differ. Moreover, knowledge play a significant role in determining power in all the other pillars, and could therefore be argued to have a foundational role. One way to limit the complexity of the knowledge pillar is to view it strictly as a resource, which is arguably a slightly simplistic view. This view is contested by Bourdieu who argued that "*The theory of knowledge is a dimension of political theory because the specifically symbolic power to impose principles of the construction of reality"* (Bourdieu, 1977: 165). This address the fundamentally interesting, but also complex question, of viewing knowledge as a resource, namely: *"Why are certain truth accepted as known while others are not? And how is this agenda of truth set and contested within the knowledge structure?"* (May, 1996: 184). Given the centrality of knowledge creation and the claim of legitimate knowledge in agenda setting within development finance, these are interesting questions. This pillar is important in providing a frame of analysis with a potential of uncovering underlying mechanism that are deemed valuable through our critical realist approach. One might even argue that understanding the knowledge dynamics are central to understanding the field of development finance.

In addition to the primary pillars the Strangeian approach argues for the existence of secondary pillars central to the analysis. Strange argues for secondary pillars such as: Transport, Trade, Energy, and Welfare. This list is not seen to be exhaustive, and secondary pillars are to be understood as a definition of an area of analysis. Hereby, these pillars are secondary to the primary pillars described above, as primary pillars are driving the motivations for actions within the secondary pillars (Revell, 2006). It is acknowledged that secondary pillars can affect primary pillars in certain cases.

Summing up, it is important to note that the theoretical understanding of power and the framework for addressing structural change will guide the way we apply other theoretical considerations in our analysis. The central parts of the Strangeian approach can be summarized to be:

Table 4

- Rejecting the state-centric approach through the acknowledgement of an increasing capability of agenda-setting by private actors. Underlining the importance of understanding the interplay between states and private actors.
- Taking a more pluralistic approach to the study of IPE with the goal of employing a more holistic/pragmatic approach to the field.
- Dividing power into relational and structural. Analysis is mainly focused on changes in structural power, as these are seen to be more persistent due to arguments resembling path dependency.
- Using four central pillars of analysis: *Money and Finance, Knowledge, Production, and Security*. Hence, breaking down a complex international playing field into four key areas of study. Allowing for a separation of factors, while simultaneously acknowledging their interdependency.
- The knowledge structure is controversial but essential, as it provides the possibility to uncover underlying mechanisms.
- A pragmatic approach to understanding who benefits from a certain structural change.

4.2.2 Who Benefits? The Relevance of Susan Strange to this Thesis and some Criticism

The ultimate question defining the framework suggested by Susan Strange is ***who benefits***? This address a wider array of questions such as: *who gets what? How costs and benefits are distributed, and who pays adjustment costs? and the struggle between these*. Additionally, these underlying questions will play a large role in our discussion of the capability of the AIIB, to contribute to aligning private and public resources to effectively guide more capital towards infrastructure in developing countries.

A central point of criticism of the theory have been the addition of the knowledge pillar, but two additional points are necessary to touch upon. Firstly, the eclectic approach has been seen to be epistemologically problematic. This is seen as less problematic in this thesis as it undertakes a critical realist approach to knowledge creation, which allow for eclectism. Secondly, the lack of an explicit approach to structural change is criticized. Strange offers some explanation suggesting that change happens through changes in technology, states, and markets, but does not succeed in explaining the dynamics of how these interact to drive change (May, 1996). This thesis will explore the usefulness of new institutionalism to provide more insights on the on institutional change as a driver of structural change. This will happen throughout the analysis of importance motivations for institutional emergence and design. Hence, changing the power structure between states and the constellation of the market. The importance of technology will be an implicit factor in understanding the market implications of increased participation from developing countries.

The four Strangeian pillars will serve as a tool to tackle and structure the complexity of power structures within development finance, while New Institutionalism will serve as the main explanatory theory for institutional emergence and design. Below the New Institutionalist analysis of the AIIB will be presented.

5. Analytical Section

5.1 Introduction to the Analysis

The starting point of our analysis is the identification of key factors driving and shaping the emergence of AIIB. From there we move on to conduct a systematic investigation of each factor in order to gain an in-depth understanding of *why and how* these factors have played a significant role in the emergence of the AIIB.

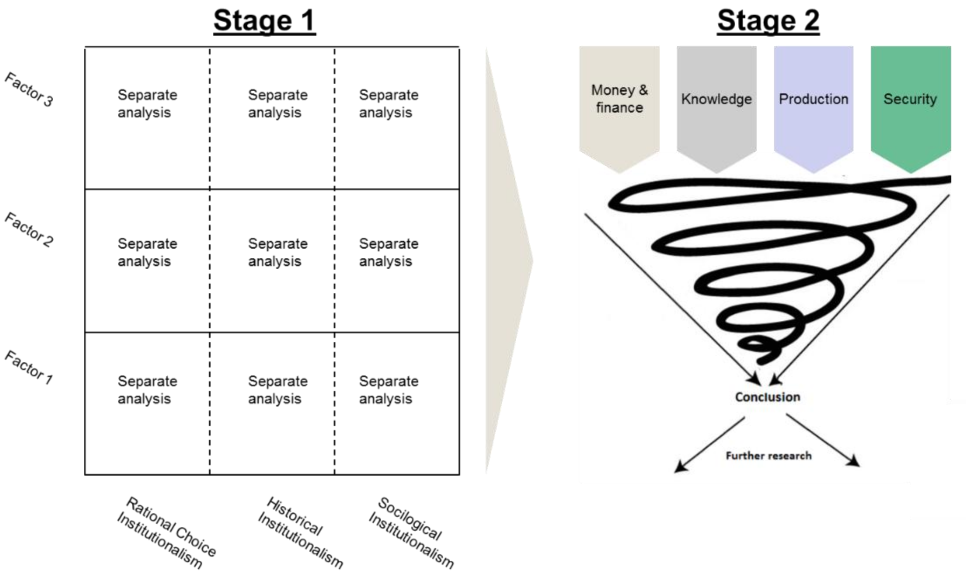
We are not the first to identify the contributing factors presented below. The identification of factors is a necessary step towards a more substantial analysis of each factor. We consider factors identified by others (both primary and secondary sources) and exercise judgment regarding their significance. Based on interviews with key individuals and examination of reports and other secondary sources, our research suggests three factors that played a key role in driving and shaping the emergence of the AIIB:

1. **Uneven Representation**: There is an uneven representation of developing countries within the current international financial institutions (IFI).
2. **Infrastructure Finance Gap**: A sizable infrastructure finance gap in developing countries in Asia
3. **Capital Capacity**: China's significant capital reserves enable it to pursue various strategies for addressing domestic and regional economic issues

These factors are essential to understand the emergence and design of the AIIB. The analysis is organized as follows:

- Description of the factor
- Stage I - applying each New Institutional perspective to the factors
- Stage II – Applying the Strangeian four pillar framework to analyze who benefits.

Figure 5



In Stage I we analyze the factors from the perspective of New Institutionalism, which allows us to answer the first part of our research question, which simplified asks *why and how did the AIIB emerge?* Followed by Stage II where we apply the Strangeian four pillars to perform an analysis of the structural power change we answer the second part of our research question *who benefits?*

Identifying Interview Respondents

Our overall target groups have consisted of three communities – policy, private sector, and academia. The policy community constitutes professionals representing governments, MDBs, and NGO's. Private sector respondents have been professionals representing an institutional investor, while academia has been scholars either representing a research institution or university.

To identify potential respondents, we relied on the following sources: Respondent's was identified and approached at two conferences. The first conference was the bi-annual Harvard Project for Asian and International Relations (HPAIR) conference at Harvard University. External funding from the Oticon Foundation in Denmark was acquired, which made attendance possible. Through participation in seminars and lectures covering the future of sustainable infrastructure in Asia, we identified three respondents.

During the second conference, the Financing for Development: follow-up to the Addis Ababa Action Agenda at the United Nations in New York, we made contact to four respondents. Furthermore, we have identified respondents at two events hosted by CBS and during one of the author's internship at the General Consulate of Denmark in New York. The rest of our respondents have been identified throughout desktop research.

The majority of the private sector respondents were interview in Phase 1 of our research process, while the majority of policy and academia respondents were interview in Phase 2. Most of the interviews in Phase 3 were with high level respondents that were not available earlier in the research process (see figure 1).

In all, we interviewed 22 respondents – eight from the private sector, nine from policy, and five from academia. See list below:

List of Interview Respondents

Community (Academia, Policy, or Private Sector)	Respondent's Job Title and Company/Organization	Selection	Date	Format	Length (estimated)
Private Sector	Partner, Goldman Sachs	Direct contact	April 28, 2016	Semi-structured face-to-face interview (low-degree)	01:43:00
Private Sector	Partner, Actis	Direct contact	March 18, 2016	Semi-structured phone interview (low-degree)	00:35:00
Private Sector	Sustainable Investment Director, Pension Fund	Direct contact	December 11, 2015	Semi-structured phone interview (low-degree)	00:25:00

Private Sector	Assistant Vice President, Compliance, Risk, and Governance	Meet at Harvard Conference (Sustainable infrastructure)	February 13, 2016	Semi-structured face-to-face interview (low-degree)	00:40:00
Academia	Professor, LSE	Meet at UN FfD conference	April 26, 2016	Semi-structured face-to-face interview (low-degree)	00:10:00
Policy	Director, Legal and Governance, China oriented NGO	Meet at Harvard Conference (Sustainable infrastructure)	February 13, 2016	Semi-structured face-to-face interview (low-degree)	00:20:00
Policy	Chief Economist, International Institute of Finance	Meet at Harvard Conference (Sustainable infrastructure)	February 14, 2016	Semi-structured face-to-face interview (low-degree)	00:25:00
Policy	Vice President, Investment Fund for Developing Countries	Direct contact	January 12, 2016	Semi-structured face-to-face interview (low-degree)	01:35:00
Private Sector	Responsible Investment Analyst, Pension Fund	Direct contact	January 12, 2016	Semi-structured face-to-face interview (low-degree)	01:20:00
Private Sector	Partner, Copenhagen Infrastructure Partners	Direct contact	January 11, 2016	Semi-structured face-to-face interview (low-degree)	01:15:00
Academia	Senior Researcher, Danish Institute for International Studies	Direct contact	April 14, 2016	Semi-structured phone interview (high-degree)	00:27:57
Academia	Team Leader, Climate Finance, Overseas Development Institute (ODI)	Meet at UN FfD conference	April 19, 2016	Semi-structured face-to-face interview (high-degree)	01:06:13
Academia	Senior Researcher, Overseas Development Institute (ODI)	Direct contact	April 13, 2016	Semi-structured phone interview (high-degree)	00:34:18
Academia	Professor, CBS	Direct contact	April 19, 2016	Semi-structured phone interview (high-degree)	00:27:54
Policy	Government Official, Trade Council, Ministry of Foreign Affairs of Denmark	Direct contact	April 15, 2016	Semi-structured face-to-face interview (high-degree)	00:16:03
Policy	Senior Executive, World Bank Group	Meet at UN FfD conference	June 6, 2016	Semi-structured face-to-face interview (low-degree)	00:27:12
Policy	Executive Director appointed by member states	Meet at UN FfD conference	April 19, 2016	Semi-structured face-to-face interview (high-degree)	00:07:00
Private Sector	Principal, Development Consultancy	Direct contact	January 15, 2016	Semi-structured face-to-face interview (low-degree)	00:40:00
Private Sector	Chairman, Development Consultancy	Meet at CBS event	May 26, 2016	Semi-structured face-to-face interview (low-degree) and email correspondence	00:05:00
Policy	Government Official, International Development, Ministry of Foreign Affairs of Denmark	Direct contact	May 14, 2016	Semi-structured phone interview (high-degree)	00:45:00
Policy	Principal Economist, European Bank of Reconstruction and Development	Direct contact	June 2, 2016	Semi-structured phone interview (low-degree)	00:30:00
Policy	Procurement Officer, United Nations Development Program (UNDP)	Met as part of internship (JBN)	April 10, 2016	Semi-structured face-to-face interview (high-degree)	00:25:00

5.2 Introduction to Stage 1 – The Purpose of the Analysis and the Identification of Key Factors

This section elaborates on key aspects central to the purpose of the Stage I analysis centered around the understanding of ***why*** and ***how*** the AIIB emerged. This section will provide additional reflections on the **factors** that will provide the structure of the analysis. Three strands of reflections will be provided in this section. Firstly, a brief recap of what is understood by ***why*** and ***how***. Secondly, reflections on our definition of the term **factor**. Thirdly, elaborate on the process of selecting and applying the factors.

The why and how

Why did the AIIB Emerge?	An analysis of why the factors have contributed to the emergence of the AIIB and thereby taking the first step to identifying the underlying mechanisms driving the process of emergence.
How did the AIIB emerge?	The ***how*** seeks to establish a greater understanding of the underlying mechanisms driving the design of the AIIB.

Reflections on the definition of the term factor – presentation of factor criteria

A **factor** is a phenomenon existing independent of the AIIB but with specific relevance to the emergence of the bank. We have defined such relevance to contain three properties:

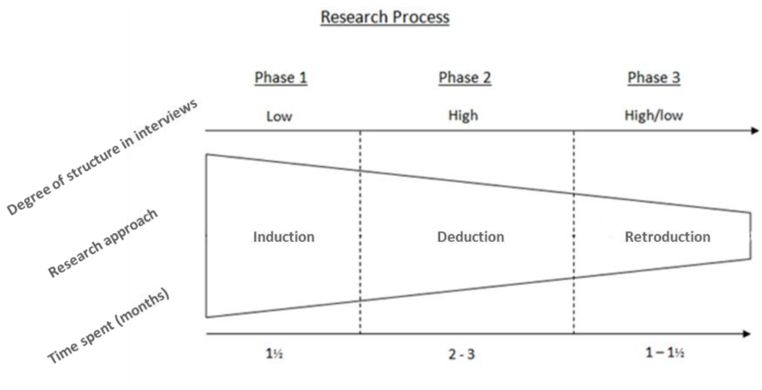
1. The phenomenon is described by experts as having a significant impact on the emergence of the AIIB
2. The emergence of the AIIB has an impact on the phenomenon - changing its nature
3. There is a consensus around the phenomenon in the field.

An example of a factor that was excluded is the Beijing Consensus. This was discussed in interviews as a potential factor driving the establishment of the AIIB, but the lack of consensus among interviewees disqualified the phenomenon as a factor. This example is interesting, as it does not disqualify this phenomenon from being discussed as an underlying mechanism, which will become apparent in our analysis.

The process of selecting and applying factors

The data used in the formulation and selection process of factors was collected through Phase 1 of our research process. Our inductive approach in this phase allowed us to gather a broad understanding of what industry experts deemed to be important in connection to the emergence of AIIB.

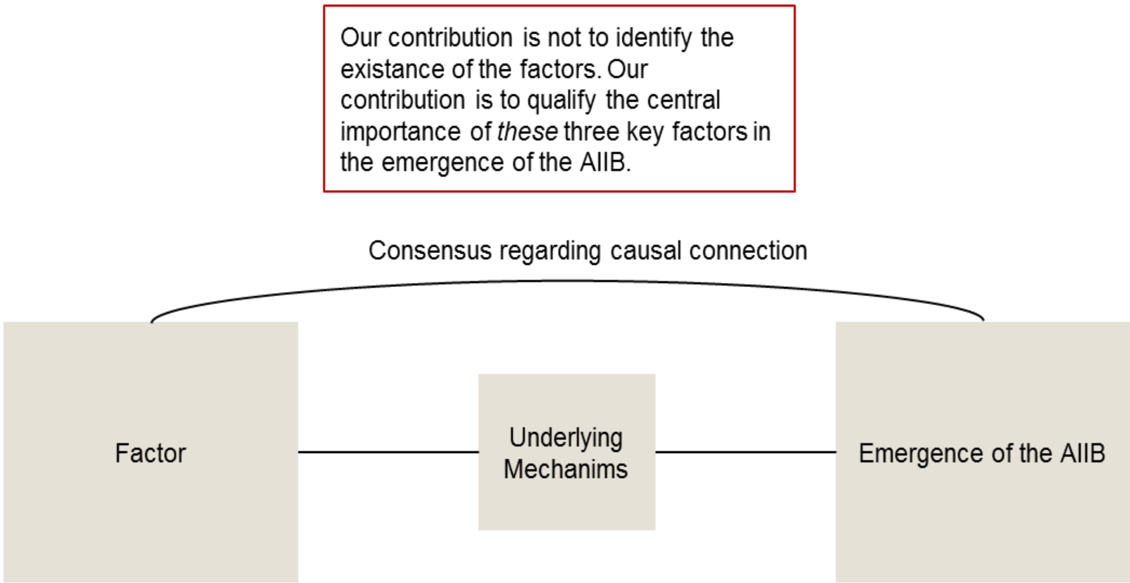
Figure 1



Our wording for each factor was decided based upon knowledge gathered at the interviews and through desktop research. Once we had a set of hypothesized factors we put them through the test of the three defining features of a factor outlined above. This means that the three factors selected are not to be seen as an exclusive list containing all potential factors. Instead, they are carefully selected on their perceived impact and the level of consensus surrounding their existence. It is not the aim of this thesis to provide a complete list but rather to analyze underlying mechanisms. This emphasizes the necessary weight of the factors, as we want to avoid discussions of consensus and existence of a given factor. Such discussions have merit in the analysis of causal mechanisms/relations but are not seen to add analytical value to the identification of underlying mechanisms. The application of factors is intended to have the following flow of logic:

1. The factors we have selected provide an analytical starting point for our research. Hence, our analytical contribution is not to provide new knowledge about the factors. Our contribution is limited to the *selection* of some key factors through applying our three selection criteria.
2. The three New Institutionalist theories are applied to the factors. This action has two major objectives. Firstly, to provide a frame for a pluralistic analysis of underlying mechanisms. Secondly, to test the explanatory power of New Institutionalism to the case of the AIIB. The contribution here is a better understanding of underlying mechanisms and an improved understanding of theoretical strengths and weaknesses of New Institutionalism.

Figure 6



5.3 Factor 1: Uneven Representation

The section below will provide some initial context for factor 1, and thereafter the analytical perspectives of New Institutionalism will be applied.

Factor 1:

There is an uneven representation of developing countries within the current international financial institutions (IFI).

The dominant institutions within the MDB and IFI system was designed between the Bretton Woods Conference in 1944 and the Asian Development Bank's (ADB) commencing of operations in 1966 (See appendix for MDB mapping overview). Changes in the economic wealth and capacity of some of the largest developing countries have radically changed the global economic outlook of the world. The current IFIs was designed for an "old" world, which is reflected in the current allocation of voting power within these institutions. Evidence for this observation is displayed in the table below.

Table 5

	IBRD	IDA	IMF	ADB	GDP
US	16.65%	10.36%	16.75%	12.71%	22.37%
Japan	7.40%	8.36%	6.23%	12.798%	5.91%
China	4.65%	2.10%	3.81%	5.459%	13.30%

Source: IBRD Official data, IDA Official data, ADB Annual report 2015, and Vestergaard & Wade, 2015

With predictions that forecast China to become the world's largest economy by 2025 (Biswas, 2015), time will only exaggerate the discrepancy between economic power and the share of votes in the old institutions. The data shows furthermore how the U.S.'s share of votes in the World Bank and IMF is superior, and likewise, how Japan and the U.S. enjoy significant control of the ADB.

Voice Reform at the World Bank

In 2009, in the aftermath of the financial crisis, G20 leaders agreed to reform the governance of the IMF and the World Bank to increase representation of developing countries. The two organizations agreed to make ratifications of capital subscriptions and apply the share of world economy as the primary criterion for countries' share of votes (Vestergaard & Wade, 2015). The implementation of reforms has contrary to the stated objectives increased developed country's voting power relative to GDP, due to the categorizing of countries seen as developed. Voting share of developing countries is therefore significantly lower than what was agreed on back in 2010; 3 percentage points lower in the World Bank and 2.6 percentage points lower in the IMF (ibid).

At first glance when looking at the numbers the World Bank reform seemed real. But as the World Bank includes several high income countries in its category "Developing and Transitional Countries", the actual picture is different. The powerful members have not allowed developing countries to increase their capital share proportionate with their share of world GDP. The two main components in determining voting share are capital contribution and share of GDP, and as a proportionate change in capital share have been denied actual changes have not had the desired impact. While a voting power parity between developed and developing countries was the stated objective, the actual picture is still 61.7 percent against 38.38 percent, respectively (Vestergaard & Wade, 2015: 6). The reform was welcomed as it addressed the dissatisfaction of the uneven representation. However, its lack of actual impact has caused frustration among many developing countries. Turning to the proclaimed reforms at the IMF proves an even graver example, as the voice reform at the World Bank after all can be argued to be a step in the right direction.

Stalemate in the IMF Reform Process

In 2010 the IMF Board of Governors agreed on a governance reform package. The stated objective was to shift 6.2 percent of voting power from developed to developing countries. The package also included a doubling of the IMFs financial resources to about $755.7bn as well as shifting two seats on the IMF board of Executive Directors from advanced European countries to emerging countries. The overall reform would have made China the third largest shareholder, after the United States and Japan, and allowed three of the BRICS to become top-10 shareholders (Brazil, Russia, and India) (Bob et al., 2015: 12). About six years after the announced reform, it has still yet to be implemented, because the US Congress is blocking the process.

Should the reform be implemented, it would still be far from aligned with the proclaimed objectives, which the IMF and the World Bank share. Developed countries would still be heavily over-represented when looking at their economic size relative to their voting power, and most of the shift in voting power would occur *within* the group of developing countries (Vestergaard & Wade, 2014).

Interview Material Emphasizing Uneven Representation

It seems clear that the dominant countries have proved unwilling to actively change the current system to create a level of influence that reflects the modern world order (Reisen, 2015; Elgin-Cossart & Hart, 2015). Interestingly, the U.S. has pushed for China and other emerging economies to take bigger responsibility in international development finance (Reisen, 2015). In regards to the lack of reforms, it does seem reasonable that a country is not willing to take bigger responsibility in an institutional setting, where the ability to affect the decision making process would not match contributions. This was framed well in interviews with scholars and former MDB employees from the Overseas Development Institute (ODI), one of the leading research institutions on MDBs;

> *"The non-borrowers have all the votes they need. They don't have the majority, but enough to control changes to the capital structure in these banks, so every time there is a need for a capital increase the non-borrowers get together and say, we are not going to give you this*

increase unless you accept all these impositions on the way the bank should be run" (ODI, interview material).

And,

"[China] is changing global macroeconomics, and the fact that we have an unprecedented economic power in the emerging economies in Asia and they wish to play a more prominent role in global economics than they have been able to previously, so that is changing global power structures and economics in that context." (ODI, interview material).

There is clearly an explicit discontent with the rigid structures of the system and a frustration around the unwillingness by the nations holding the majority of voting power to enforce actual change - a view supported in our interviews:

"China would like to be able to contribute more to these banks by an increase in its capital share, and thereby an increase in its voting share. But the other countries have not allowed to do so. And this is played out also especially in the area of infrastructure, because a lot of these environmental and social safeguards, rules put in place by the World Bank especially by the Pelosi Amendment, Nancy Pelosi pushed it though the US Congress, and some other rules, well, basically they haven't funded a hydropower dam in I don't know how long" (ODI, interview material).

The lack of influence on the conditionality following loans is a specific issue causing frustration, as it forces developing countries to follow inflexible frameworks. These frameworks are often viewed to fail in considering country-specific issues, and the length of project preparation time due to increased bureaucracy in development procedures.

Many scholars see the AIIB and other new institutions as a result of this growing impatience around reforms that substantially address the issue of uneven representation (Renard, 2015; Xu & Carey, 2015; Elgin-Cossart & Hart, 2015; Die, 2015; Humphrey, 2015; Beaulieu & Dobson, 2015; Biswas, 2015; and interview material).

In the following, factor 1, uneven representation, will be analysed through the lens of the three New Institutionalist perspectives, which will reveal subtler and latent motivations for the emergence and design of the AIIB.

5.3.1 Rational Choice Institutionalism (RCI) Perspective

Emergence

The 2008 financial crisis was somehow a welcomed event for developing countries in regards to expressing their dissatisfaction with an uneven representation within current IFIs. As developed countries were lacking liquidity, they were forced to interact with greater inclusion towards developing countries, particularly China. Although China is a member of the current IFIs, it lacks actual influence as shown above.

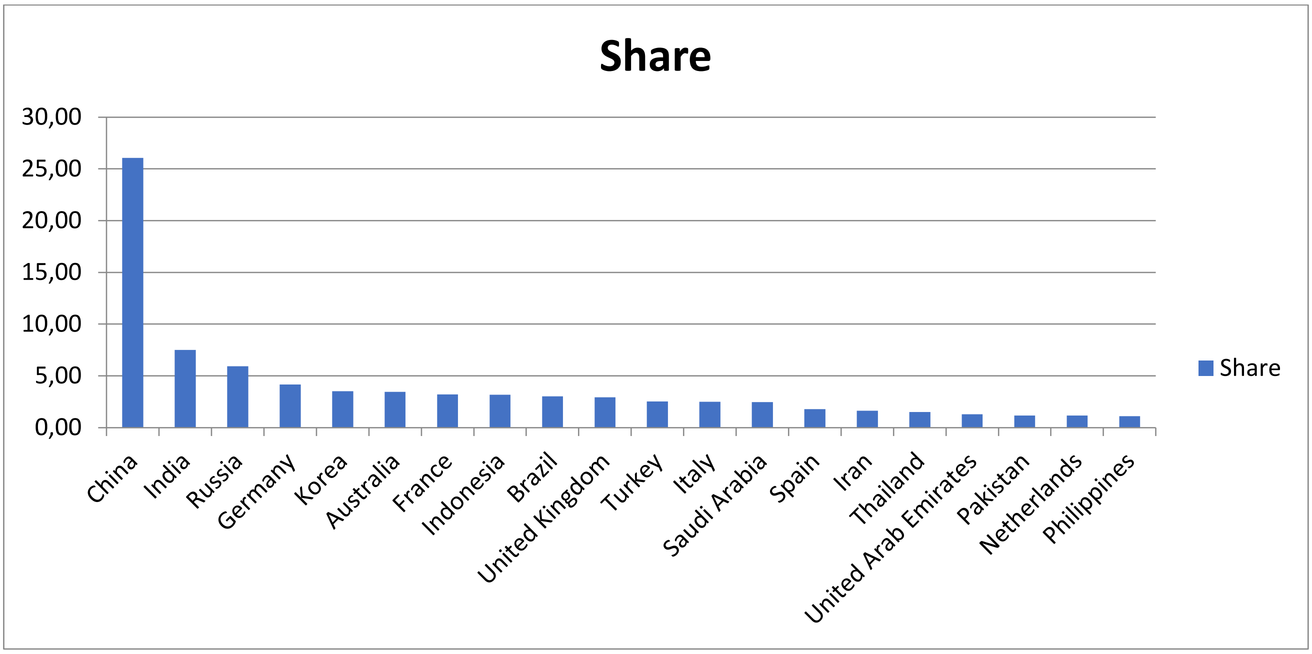
From a RCI perspective, China used this opportunity to initiate a process aimed at achieving certainty around whether the Bretton Woods institutions would be able to facilitate their interests ahead. As it is not without costs to make institutional changes, China's initial push to reform the existing institutions can be seen as a rational cost-benefit effort to minimize costs. Then as a consequence of the aforementioned lack of real voice reforms at the World Bank and the IMF, China has (with the launch of the AIIB and other Sino-centric institutions) concluded that their utility is not to be maximized within the current institutional regime. Furthermore, the institutional change we have witnessed, with the AIIB as the prime example, is the result of China's opportunity cost assessment. This assessment includes an overview of the costs associated with the skewed voting power equilibrium as well as an evaluation of the cost of change vs. the opportunity cost of status quo.

Design

Even though the AIIB turned out to be much more than just a regional MDB in the light of its membership structure, China has insured that the interests of developing countries are pivotal. By securing that regional members will hold 75 percent of the capital stock, China has made sure to avoid the situation experienced within the old institutions. Allocation of votes is based on each member's[5] share of the world economy, as was also the claimed objectives with the voice reforms described above. The figure below shows the allocation of voting shares among the most powerful members:

[5] Non-regional members subject to a limit, see section XX

Figure 7



Source: Center for Global Development

As the AIIB is a regional infrastructure bank, it makes sense from a RCI perspective to secure regional supremacy in the allocation of voting power. This is emphasized with the effective veto power that China enjoys at the bank. To explain why China then pursued membership from many of the countries blocking its own opportunities within the existing institutions, one has to especially look at the European members' effect on the costs of loans (achieving high credit rating).

Furthermore, to ease the costly bureaucratic procedures in the decision making process of project selection, the AIIB applies a non-resident model regarding the Board of Directors (AIIB, 2016c; Griffith-Jones, 2016: 19). By this provision, the management team is empowered to enhance operational efficiency internally in the AIIB, which is aligned with the goal of being a *lean* cost-efficient institution (AIIB, 2016c).

Sum up of findings of using an RCI perspective on Factor 1
Emergence - The AIIB is emerging as opportunity costs and a utility limitation, associated with uneven representation within the current institutions, are surpassing the costs of institutional change. - China and the other developing countries have an interest in increasing their power on regional decision making.

Design - The bank is designed to increase operational efficiency and limit transaction cost to maximize the utility of capital.

5.3.2 Historical Institutionalism (HI) Perspective

Emergence

Within this perspective, power structures and inequality are the primary drivers for institutional change – with emphasis on the effects of inequality. To explain the emergence of an institution like the AIIB, the HI perspective would examine how inequality has been structurally and functionally exercised over time.

As developing countries within the last decade have increased their share of the global economy, time has also increased inequality between developed and developing countries within the old institutions. The lack of reallocation of voting power has led to a latent conflict, which now becomes apparent through the initiation of a structural change. The quote below highlights the motivations behind this change:

> *"(...) since the established multilateral architecture doesn't necessarily always serve their interests to resonate with their priorities, there is a wish to see institutions that are more reflective of their needs and interest created and support by themselves. And that have particularly had a strong sentiment politically for some time among the Asian countries."* (ODI, interview material)

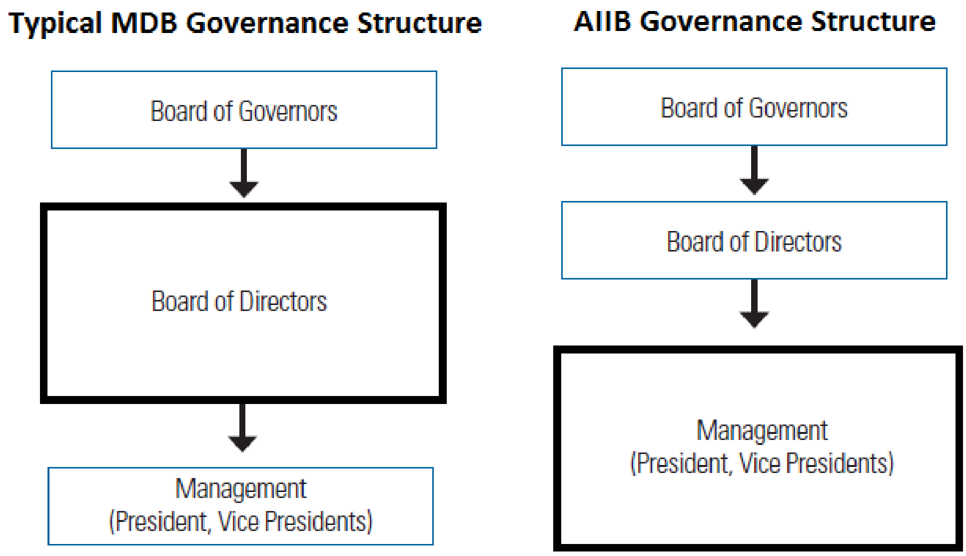
As expressed, the dissatisfaction also has a temporal dimension, which the HI perspective subscribes great explanatory power. Crucial events, such as the unsuccessful voice reforms, show how historic power constellations are deeply embedded in the structures, and how difficult it is to escape institutional path-dependency. In addition, HI also acknowledges that developments of ideas are impactful. Again, the temporal aspect is emphasized, which fits with the underlying development of a specific Chinese approach to development (thoroughly described in the background section) then materializing in the creation of the AIIB. Therefore, the emergence of the AIIB can also be seen as a natural consequence of the maturing of a different approach to development. This analysis hereby displays the eclecticism of the HI perspective, as it does not ignore the power of ideas in shaping institutions either the structural power to sustain or re-alter inequality.

Design

From the HI perspective, the governance design of the AIIB is a result of China's desire for an MDB more reflective of their understanding of such institutions, and the need to fit into existing historic structures. Let's start with the latter. As the AIIB is a multilateral institution and aimed at coexistence, and especially cooperation with existing MDBs during the first years of operation, there is a pragmatic need to fit into existing structures. This clearly shows the strength of path-dependency within an institutional system, as the AIIB illustrates how significant change is difficult. It is important to decipher that as the AIIB is proclaimed to be a best practice bank by the Chinese themselves, we still truly don't know how much of a political statement it is vs. a true conviction that the structure is their desired form. This displays how HI can help us understand how actors seek to consciously navigate existing power structures.

As noted before, there are important diversions from most existing MDBs governance structure, especially when it comes to the amount of power subscribed to the operational level. Operational power, which is more pragmatic in its nature, takes precedence from a Chinese perspective. While the center of gravity is to be found around the more political power within the existing institutions - at the Board of Directors. The illustration below shows how power is centered at the operational level of the governance structure, which the sheer size of the different levels illustrates:

Figure 8



Source: Authors own

This ultimately means that you could argue the AIIB is less about representation and more about operations, which the historical experience of uneven representation within the old institutions, has taught the Chinese architects behind the AIIB.

Sum up of findings of using an HI perspective on Factor 1
Emergence - As economic power shifts, inequality (uneven representation) becomes exaggerated to the extent that the AIIB emerges as a response. - The lack of historic change is a consequence of deeply embedded power structures that suffers from path-dependency
Design - The governance design of the AIIB can be traced to the idea of governance from a Chinese perspective, which allocate power within institutions from a more pragmatic and operational perspective.

5.3.3 Sociological Institutionalism Perspective

Emergence

As the SI perspective places legitimacy at the center of the analysis, the factor, uneven representation, becomes an interesting subject. Basically, it can be argued that lack of *legitimate* reforms addressing uneven representation within the established institutions has sparked a cultural shift that created the *legitimacy* to create new institutions. This pressure comes from the increased share of the world economy placed in the hands of developing countries. It makes the current representation a legitimate issue to address with reference to the Western world's own discourse around legitimate representation. What this in more detail has caused, is a legitimate window of opportunity for China to test out its own idea of development in a multilateral context. The discrepancy between the Chinese and Western "frames of meaning", referring to the approach to development, are still apparent with precedence to the Western. But as the U.S. obstruction of legitimate reforms has undermined the norms and values advocated by these institutions, a new institution has emerged as a reaction and to fill out what could be called a "legitimacy gap" in the development field.

Design

The SI perspective furthermore reveals interesting underlying motives regarding the design of the AIIB. The Chinese are not "suffering" from a democratic legacy, which shaped the governance design of the old institutions. This makes it possible for them to make certain different, but *legitimate* maneuvers, when it comes to the design of the governance structure. The AIIBs operating context is still based on a strong normative foundation not easily changed. The multilateral context the AIIB places itself within, is exactly the context where legitimacy in the development space is created. From a SI perspective, this explains why a regional MDB as the AIIB has sought membership across continents (Brookings, 2015). To make this institution a successful one, it needs to distribute its ownership among most importantly normatively different stakeholder to create broad legitimacy around the operations of the bank – and therefore legitimacy around operations more reflective of the Chinese approach to development. As such, the SI perspective provides a strong explanation for the significance of becoming positively embedded in a general perception of appropriateness.

Sum up of findings of using an SI perspective on Factor 1
Emergence - Lack of legitimate reforms from a Western normative perspective has created a window of opportunity for China to materialize its own idea of multilateral development into an institution – the AIIB.
Design - The governance structure of the AIIB reflects the balancing of culturally different approaches to decision making, while the high degree of multilateralism is the socially accepted way to achieve institutional legitimacy in the development field.

5.4 Factor 2 - Finance gap

The following section will describe factor 2 - the finance gap. In our research we have observed that the finance gap is central to the emergence and design of the AIIB. The purpose of this section is to introduce the factor and give the reader sufficient background information to understand how this specifically relates to the case of AIIB.

Factor 2:

A sizable infrastructure finance gap in developing countries in Asia

Definition of key terms for factor 2	
Infrastructure	When using the term infrastructure, we refer to what could be termed as public goods infrastructure: This means infrastructure that is non-excludable and non-rivalrous. Examples of sectors covered by the

	AIIB are: Energy and power, transportation and telecommunications, rural infrastructure and agriculture development, water supply and sanitation, environmental protection, urban development and logistics.
Finance Gap	The finance gap refers to the lack available finance for infrastructure that is essential to provide basic services and channel economic growth. The gap refers to a lack of financial capital to supply a sufficient level of infrastructure as a public good, as is described above. Sufficient infrastructure is defined as securing a foundation for economic growth.

The magnitude of the infrastructure finance gap

Infrastructure is central to the success of all major development tasks, as it provides a foundation on which more prosperous societies can exist. The current infrastructure is estimated differently by various sources.

Figure 9

Estimates of infrastructure needs – Asia and Global

Source	Time horizon	Regional focus	Amount (USD tr)
ADB	2010 - 2020	Emerging Asia	8.5
HSBC	2010 - 2030	Emerging Asia	11.5
McKinsey	2014 - 2030	ASEAN-5	7.0
B20	2015 - 2030	Global	57.0

Source: Deutche Bank, 2016

As seen above, estimates vary in inclusion of countries and time horizon. This should be compared to a current annual investment of roughly $1bn (Reisen, 2015; Humphrey, 2015). This clarifies that the region (Asian developing countries) is in need of new investment sources, as it is unrealistic that the current institutions can close this gap. A large part of the world's current infrastructure projects is financed by government infrastructure budgets, Asian government spending estimated to $500bn-$600bn (Reisen, 2015). Traditionally a need for additional infrastructure finance would be accommodated through an increase in government spending, but such possibilities are limited by fiscal constraints. Moreover, the World Bank has reduced its initial strong focus on infrastructure investments to amount to only 30 percent of the banks overall activities (Reisen, 2015). The number of tasks currently undertaken by existing MDBs makes them incapable of increasing their infrastructure contribution significantly.

The current institutional vacuum

In spite of the World Banks change of objectives, the MDBs are uniquely positioned to undertake the challenges of investing in infrastructure in developing countries. Traditional public finance is limited by fiscal constraints, while private finance sources are often unable to undertake the non-commercial risks and navigate systemic market failures existing in the region. The smaller poor countries such as Myanmar, Cambodia, and Laos have a large need for investments to successfully emerge from years of political and economic isolation (Beaulieu & Dobson, 2015). This leaves a vacuum for MDBs to provide direct finance, crowd in private finance through mitigating market failures by issuing guarantees, or increase project quality through development support (Reisen, 2015).

Interview & Speech Material Emphasizing the Finance Gap

We have interviewed leading members of MDBs, but due to confidentiality we have chosen to include public statements from recent speeches to document their stance on the finance gap. The busy schedules of senior officials have limited our ability to ask follow up questions and we acknowledge that public statements tend to be more general in their nature than interview data. The need for an institution like the AIIB is acknowledged by industry experts and the leader of the AIIB, Jin Linqun. Additionally, the World Bank, EBRD, and the ADB has invited the new institution to collaborate on solving the tasks ahead (Ashurst, 2016). This desire to collaborate is apparent in the project proposals currently available, where three of four projects is in collaboration with the aforementioned institutions. The following quotes emphasizes was has been noted above:

Table 5

ODI, Interview material	*"(A reason for the emergence of AIIB) is related to a very real desire, these countries have to expand their existing infrastructure stocks.".*
DIIS, Interview material	*"It is an alternative source of financing compared to some other institutions and it is not clear what safeguards on environmental issues, social issues, labor issues and due diligence would be like but China is cooperating with ADB and World bank on designing and adopting these measure so on that point I don't think they are that competitive. I mean it is an*

	alternative source of finance and there is a huge gap in financing for infrastructure".
President of the AIIB, Jin Linqun (Brookings, 2016)	*"The Asian market, either the goods market or the assets market has remained fragmented, partly due to the connectivity problems, which certainly is due to the inefficient infrastructure. This has led to the persistent poverty, high fertility rate and expectation of old age (sic) in security, low level education and environmental degradation due to the poor's desperate efforts to wrestle a meager living from the fragile environment".*
President of the World Bank, Dr. Jim Yong Kim, (FT, 2016)	*"If the world's multilateral banks, including the new ones, can form alliances, work together, and support development we all benefit from — especially the poor and most vulnerable. (...) I will do everything in my power to find innovative ways to work with these banks".*

The AIIB is, among other motivations, a reaction to the aforementioned vacuum, which welcomes new actors to contribute with additional financial capital. Hence, direct competitions on projects are unlikely in early stages, given the collaborative agenda of the AIIB and existing institutions (Ashurst, 2016; Elgin-Cossart & Hart, 2015). The successful coexistence of the "new" and "old" institutions is dependent on a certain alignment of governance measures to avoid counterproductive competitive behavior (Humphrey, 2015b). Concerns have been raised around rivalry between MDBs, which could spark geopolitical tensions, potentially leading to an unhealthy competition on project safeguards. However, the large number of developed countries committed to the AIIB and China's initial open approach has created some comfort around the stated collaborative agenda (Biswas, 2015).

The magnitude of the finance gap suggests that it is necessary to leverage public finance through investing in ways that enable private finance to accompany public investments. This could allow for a larger "bang for the buck" of MDB finance. Institutional investors are uniquely placed to engage in long-term infrastructure finance, and therefore could be an interesting partner in various fund structures. This point is emphasized by the AIIB's President, Jin Linqun:

> *"I think our efforts to promote private sector development would be a very important part of our strategy. There are two things you need to think about. First of all, the level of institutional capability, which is the defining factor for any country in a particular historical stage. (….) (Secondly,) I think we can develop the capability of the private sector. So, I believe by working with the public sector, and also, at the same time, to promote the institutional capability of the private sector we can move towards greater future collaboration"* (Brookings, 2016).

It is acknowledged by the bank that an effective collaborative relationship with the private sector requires persistent work. The existing knowledge gap between the public and private sector was supported in our interview with a Danish representative from the Ministry of Foreign Affairs, who attended the Addis Ababa conference[6] last year. The representative reported the existence of a misaligned perception of the current investment possibilities. This misalignment was driven by a lack of mutual understanding, which has led to inefficient collaboration between the policy community and the industry. On a positive note, the initial design of the AIIB allows for more private sector interaction than existing MDBs (Lim & Mako, 2015)[7].

Stage 1 Analysis of Factor 2

The purpose of the following section is to analyze factor 2 from the three institutionalist perspectives. The objectives of this analysis is: 1) Gain a deeper understanding of how underlying mechanisms connected to the finance gap contributed to the emergence and design of the AIIB 2) Evaluate the explanatory power of each New Institutionalist approach and if they can borrow elements from each other.

5.4.1 Rational Choice Institutionalism (RCI) Perspective

Emergence

The lack of an institutional capacity to provide credit leads to a current undersupply of finance for infrastructure in Asian developing countries. The increased need of such finance has changed the institutional equilibrium within the region. This is driven by an inability of local governments to sufficiently leverage their public budgets, as they suffer from a limited access to finance from

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[6] See appendix X

[7] See a further discussion of the private sector involvement in section X

existing institutions and the financial markets. Moreover, rigid policy-loans and slow bureaucratic processes implemented by existing MDBs have contributed to a rise in transaction cost for borrowing nations. A lack of efficient alternative solutions has raised pressure for an institutional response.

> *"Say what you will about the environmental impact of these (projects), (...) developing countries really need electric power (…) Countries say, we really don't want to deal with that, we can't deal with that, we need to get the money quickly and get these projects going. And so the banks are losing relevance in these areas."* (ODI, Interview material).

From an RCI perspective the distorted institutional equilibrium has created a demand for institutions that can deliver faster action and operate with a larger degree of pragmatism in their approach to financing projects. Such an approach could lower transaction cost and the AIIB can be seen to emerge as the cost of creating a new institution is exceeded by the cost of accepting status quo. China has this type of operational experience through the operations of their policy banks, and are therefore well positioned to lead the emergence of an institution intended for a high-pace development environment. The motivation for China to undertake such a task is rooted in the desire to optimize their economic significance within the region.

Design

The bank is designed to limit transaction costs through a Lean, Clean, and Green modus operandi (AIIB, 2016e). This is a response to the slow bureaucratic processes of existing institutions, which raise administration costs. Additionally, these processes have made MDBs an undesired partner for private sector investments. The bank seeks to limit political transaction costs through increasing the decision making power of developing countries. Currently developing countries often stress that policies enforced in connection with loans from IFIs are inconsistent with their domestic initiatives (Bob et al., 2015). The AIIB is designed to limit the political transaction costs through employing country-specific strategies in loan giving. The bank has also made conscious efforts to achieve a satisfactory credit rating in order to create an economically efficient institution. A key strategy to achieve this has been to construct a strong capital structure and create a solid managerial foundation[8]:

[8] See appendix

> *"First of all, this is the bank with the highest ratio of paid in -- 20 percent paid in capital (...) We do not reject any nationals, even if their countries are non-members. We don't reject the professionals of the highest caliber, just because of their passports. We don't reject any companies to help develop the infrastructure, just because their countries are not members. (...) We do not have the track record of AIIB as an institution, but we enjoy the track record of individual managers."* (Brookings, 2016).

A Danish lead negotiator from the MoFA, described the AIIB as a best practice bank. This is envisioned in the management team, which consists of a diverse set of internationally recognized experts in their respective fields. This team can contribute with considerable experience in creating economically sound operational practices. The initial design of the bank is structured to be lean with low administration costs, building the operational capability to act faster than existing institutions. This can be seen as a rational response to the challenges existing in the region. Additionally, this structure can be seen as an institutional response to engaging the private sector by providing conditions more conducive for cooperation.

Sum up of findings of using an RCI perspective on Factor 2
Emergence - The AIIB emerges as an institutional response to provide a more efficient distribution of international development funds into infrastructure in Asia
Design - The AIIB seeks to limit the political transaction costs through more country-specific loan requirements - The AIIB seeks to limit the economic transaction costs through reducing administration costs and reducing bureaucratic investment barriers - The AIIB provides an organizational policy that is more conducive to foster future collaboration with the private sector, enabling considerable leverage of public finance.

5.4.2 Historical Institutionalism (HI) Perspective Emergence

Today most Asian countries are in need of growing their infrastructure stock to increase the connectivity across the region. It has led to a comparison between the infrastructure support provided by the Marshall Plan and the Bretton Woods institutions. The goal back then was to reduce inequality across Europe through rebuilding the infrastructure to reinstall the foundation for future economic growth (Sekine, 2015). Similarities can be drawn to the infrastructure need that has to be accommodated across Asia in order to lift people out of poverty and to create sustainable growth (ODI, interview material). Therefore, a central motivation behind the emergence of the AIIB is to reinstall a strong focus on infrastructure through creating an MDB - the type of institution originally designed to undertake such a task.

The aforementioned Danish representative from MoFA also stressed that the perceived success of China's historic experiences with infrastructure gave Chinese officials great confidence during negotiations. They strongly felt that their historical track record proved that they possessed a set of capabilities empowering them to take a leading role in defining the structure and operations of the AIIB (MoFA, interview material). Applying an HI perspective to analyze China's confident behavior, would suggests that China is addressing a power inequality in the global economy. This is caused by the improved economic and intellectual means, which has given China the perception of having the ability to challenge historic power relations. China's domestic experience with development of large scale infrastructure provides a track record that can increase their perceived legitimacy. The idea that China is considered a capable actor was confirmed by the number of developed countries who joined during the negotiations of the substance of the AIIB (Industry expert, interview material)

Design

The World Bank's decision to limit its infrastructure investments was a consequence of emphasizing other "softer" aspects of development. This has brought a major change to the institution, as it had to obtain a more diverse set of skills. Solving more diverse tasks have grown the need for internal knowledge production. In order to store and create the knowledge created the institution has greatly grown in size. The demand for the World Bank to undertake a more diverse set of development tasks has led to a lack of investable resources for infrastructure. This type of policy pressure has eventually led other MDBs to follow this trend. The HI perspective allows us to uncover the large degree of institutional isomorphism that has affected the MDN community (Humphrey, 2015). Institutional isomorphism relates to the fact that institutions within the MDB community share certain characteristics. When institutions are affected by similar external power pressures they tend to experience a certain degree of convergence in their functionality (DiMaggio and Powell, 1983). This effect of existing structures is already felt at the AIIB:

"I think there might have been an initial feeling that they could reinvent the wheel, but they are running up against the same issues that all the other banks have and are running up against" (ODI, interview material).

A good example of the effect of institutional isomorphism is the capital structure of MDBs. Here all MDBs share a strong reliance on financial markets, which decrease their ability to take on the risks of providing loans to least developed countries (ODI, interview material). Even MDBs attempting to implement structures limiting this dependency, as exemplified by the Latin American CAF, has eventually been unable to sustain this practice (Humphrey, 2015). Riskier projects are being undertaken by development funds, which have to be replenished by paid-in capital from governments. From an HI perspective this becomes an issue regarding the finance gap, as the existing structural establishment makes governments unable to provide sufficient capital. Even if China had unlimited capital they will not be able to supply it through the MDB structure, as such actions would undermine the voting share of other member states. Hence, states would not join an institution where China would be able to independently make all decisions. A major operating trait of the MDBs is also that they are capable of financing their own operations through the financial markets. This creates certain operational constraints for MDBs, which make them unable to fulfill their fullest potential (Humphrey, 2015). Furthermore, the conservative approach of MDBs has contributed to limit their ability to find solutions for scalable ways to cooperate with private finance (ODI, interview material).

The AIIB is intended to be a state of the art MDB. Interestingly, the design of the new institution signifies an effect of being embedded in existing structures. This directs the design of the AIIB towards a resemblance of existing institutions. Two key findings suggest a degree of institutional isomorphism in the access to finance:

- The governance policy of the bank has been designed in close collaboration with experts from existing institutions that reflects expectations of the current development community (ODI, interview material)
- The capital structure is limited by being subject to the scrutiny of rating agencies and potential historic biases in risk perception (Humphrey, 2015; Kawai, 2015).

This means that through using the HI perspective, it becomes clear that while the AIIB addresses the finance gap, it also faces historic barriers created by systemic power structures within the financial system. But this new Sino-Centric institutional constellation could be seen as a first step in addressing historic barriers constituting the finance gap.

Sum up of findings of using an HI perspective on Factor 2
Emergence - The AIIB is an institutional response to reintroduce a focus on infrastructure at a multilateral level, as existing institutions have moved away from their historic focus on infrastructure - China's success in leading the establishment of this institution suggest the ability of China to drive change in existing power structures within North-South development finance
Design - The AIIB is subject to institutional isomorphism, especially in terms of governance and capital structures - emphasizing the effect of path-dependency on institutional design.

5.4.3 Sociological Institutionalism Perspective Emergence

The emergence of the AIIB can be seen as a result of a finance gap creating a window of *legitimacy* for a South-South MDB to evolve. The existing institutions have lost *legitimacy* with local governments through rigid policies, forcing regimes to enforce often undesired policies. According to a Danish official who attended the Addis Ababa conference, there is a dissatisfaction among developing countries with the dominant position of non-borrowing countries in the existing development institutions (MoFA, interview material). However, non-borrowing countries are justifiably worried that without stringent policies, the unintended environmental and social consequences of infrastructure projects will increase.

So, three interesting socialization processes are happening and contributing to the emergence as well as the design of the AIIB. Firstly, cultural norms in non-borrowing countries lead to a pressure for a stronger focus on limiting unintended consequences in relation to the projects. This has been evident in the strong discussions on the financing of coal-fired power plants, which has been an area where non-borrowing countries has exercised strong pressure for borrowing countries to act *appropriately* (MoFA, interview material). Secondly, developing countries are pushing for new solutions with a stronger understanding of their needs and domestic societies (Nakhooda, 2016). Thus, the South-South nature of the AIIB creates initial trust and legitimacy through a sense of mutual understanding. Thirdly, the global perception of China is changing from being perceived as an expert in fast but illegitimate development, to a provider legitimate development through acting appropriately and promoting of green growth (Sun, 2015).

Design

Southern actors, especially China, have gained legitimacy due to the fact that 57 countries, including large powerful developed countries, have joined the AIIB. This has happened through an outflow of not only its own economic and intellectual capacity, but also through a sense of urgency that has infiltrated the global development finance community. This has instilled the perception that the task of reaching the goals will require all countries, especially an actor like China, to contribute to these efforts. Therefore, many developed countries have become members of the AIIB, with the desire of securing a degree of control and the ability to apply direct pressure (voting power) through participating in negotiations.

A Danish lead negotiator emphasized that while Denmark's economic presence might be relatively insignificant, the country brings a significant symbolic stamp of approval to the AIIB. Securing the participation of countries that are perceived to have strong values is essential to the AIIB, and China, in gaining international legitimacy. The SI perspective stress the importance of this kind of "friendship", as it signifies an acceptance of the institution acting according to a logic of appropriateness. Accepting demands from developed country negotiators is therefore expected, as cooperation is a deliberate goal:

> *"The Bank supports the three aims of the Paris Agreement of December 2015 to strengthen the global response to the threat of climate change, which are related to mitigation, adaptation and the redirection of financial flows."* (Nakhooda, 2016).

Regarding the borrowing countries, the bank achieves legitimacy by being perceived as an institution that understands and values borrower needs. This pushes the bank towards a pragmatic country-specific approach, which will take the given needs of a specific country into account. To stay within the climate example from above, the following excerpt from the bank's policies emphasizes an attention to borrowing country needs:

> *"In the context of sustainable development, the Bank stands ready, through its financings, to assist its Clients in achieving their nationally determined contributions, including through mitigation, adaptation, finance, technology transfer and capacity-building."* (Nakhooda, 2016)

As the success of the bank depends on legitimacy from both borrowing and non-borrowing countries, it will inevitably create tradeoffs where the perception of acting appropriately differ between stakeholders. This suggests that the bank will have to obtain stakeholder satisfaction through effectively implementing an acceptable balance between pragmatism and sustainability. The legitimacy within the broader stakeholder community is central in avoiding cultural controversy. Legitimacy becomes persistent through acting according to the logic of appropriateness. This balancing act is of large importance, as the bank could play a central role in starting an integration process that will increase the collaboration between the North and South. This could eventually serve to align incentives in global development. An example of China's adoption of the global climate narrative can be seen in their impressive shift in domestic focus on sustainability (interview material)

Sum up of findings of using an RCI perspective on Factor 2
Emergence - The legitimacy of the AIIB is obtained through managing the potential tradeoff between pragmatism and sustainability. This has to allow both borrowing and non-borrowing countries to perceive the AIIB as acting appropriately - The AIIB contributes to the ongoing socialization process that is altering the global perception of China towards a legitimate actor in international development finance.
Design - The broad membership constellation of the AIIB could contribute to an alignment of incentives. Thereby, it will increase the basis of mutual understanding and bridge the North-South divide by enabling more effective use of global financial resources.

5.5 Factor 3 – Capital Capacity

The following section will describe the third identified factor – the capital capacity of China. In our research we have observed that the following domestic circumstances within China is central to the emergence and design of the AIIB. The purpose of this section is to introduce the factor and give the reader sufficient background information to follow our analysis.

Factor 3:

China's significant capital reserves enable it to pursue various strategies for addressing domestic and regional economic issues

The experts interviewed for this thesis interpret the establishment of the AIIB and other new institutions as China's mean to achieve three main objectives. These objectives will be briefly introduced below.

Investing Capital Reserves in Regional Growth

China is looking to invest its large currency reserves in regional infrastructure to gain a better return than current investments. Additionally, this type of investment contributes to real economic growth in the region. China is the country with the largest currency reserves globally - estimated to approximately $3.8tn (Mourant, 2015).

Table 6

Rank	Foreign currency reserves (end-2014)		
	Country/Region	Reserve ($bn)	Share (%)
1	China	3,843.0	33.13
2	Japan	1,260.5	10.87
3	Saudi Arabia	732.4	6.31
4	Swiss	545.4	4.70
5	Taiwan	419.0	3.61
6	Russia	385.5	3.32
7	South Korea	363.6	3.13
8	Brazil	363.6	3.13
9	Hong Kong	328.5	2.83
10	India	320.6	2.76
32	South Africa	49.1	0.42
	BRICS	4,961.8	42.77
	Overall	11,600.6	100.00

Source: Mourant, 2015

These currency reserves are mainly invested in treasury bonds in developed countries, which given the current economic situation are yielding very limited returns (Bob et al., 2015). Investing even a small portion of the reserves in infrastructure could benefit real growth in the region and contribute to an expansion of the regional market.

Promotion of Domestic Companies

Industry experts argue that the AIIB is a strategic move to promote Chinese domestic industry (DIIS, interview material). The purpose of this strategy is to expand commercial opportunities in high value added sectors. This will allow international markets to absorb domestic overcapacity and allow Chinese companies to continue to refine their capabilities in these sectors. Such a strategy is to be implemented through indirect promotion of domestic companies. The procurement policy of the bank outlines a fair and transparent process, but a tentative suspicion among experts emphasize the risk of Chinese companies to obtain an indirect competitive advantage in the bidding process (Industry expert, interview material). Chinese scholars have made comparisons between the task presented in the Asian region and the task of rebuilding European infrastructure through the Marshall Plan. These scholars have emphasized how the financial support provided by the program helped boost U.S. exports (Sekine, 2015). It is argued that a similar boost of Chinese export will occur if the AIIB is successful. China already has considerable infrastructure related export to AIIB members, the top three being: Singapore ($5,2bn), Germany ($2,6bn), and Vietnam ($2,5bn) (Sekine, 2015). But increased economic ties obtained through AIIB-loans are expected to increase this type of exports.

Improving Chinese Influence in Global Markets

Scholars argue that China is using the AIIB as an initial step to increase its legitimacy as a global financial actor. The pursuit of this strategy involves promoting the Renminbi (RMB) through infrastructure investments. China's cooperative approach suggests a serious attempt to become a central actor in international development. The first step in pursuing such a strategy is to become a leading actor in an internationally recognized financial institution that can contribute to leverage China's international political weight. The provision of RMB-denominated loans by the AIIB could provide a vehicle for further internationalization of China's currency (Kawai, 2015).

Interview Material – Chinese Promotion of Domestic Interests

The success of the AIIB is widely agreed to be a positive contribution to the Chinese economy. State-owned enterprises (SOE) have traditionally been growth engines for the economy, but these companies are suffering from an inability to increase domestic infrastructure demand (Downs, 2011). The capacity of these companies has been raised through stimulus packages and with demand slowly becoming normalized, new markets are essential. This was noted by Senior Researcher at DIIS[9]:

> *"If China can realize this vision it would be a big boost to the companies (....) And many of the participants to these projects would be state owned enterprises. They would not exclude private companies but state owned enterprises have problems making a profit so they also have to look for new markets and new opportunities"* (DIIS, interview material).

A Professor at the University of Copenhagen expanded this argument by adding that infrastructure is an area where China has strong capabilities and therefore are in a favorable position to win contracts. Chinese companies have been instrumental in lowering prices of various project inputs, e.g. solar cells, which could prove beneficial for sustainable development. To provide a broader acceptance of the use of Chinese companies it is necessary that construction quality is held to high standards. However, Chinese companies should expect competitive bidding on contracts as the implementation of procurement policies will be subject to intense scrutiny by developed country members. Developed countries are expected to advocate strongly for fair and transparent bidding processes. Both experts are positive about the idea of collaboration between Chinese and foreign companies. The Senior Researcher at DIIS shared the following observation in our interview:

> *"I went to a seminar by one of the biggest construction companies in Denmark and they have collaborated with Chinese companies and won international bids so their tech competence and their brand and maybe also the service that is packaged, could give Chinese companies a boost."* (DIIS, interview material)

As such, a general interest of expanding markets through collaboration is expressed through our interviews. The interview with a representative from the Danish MoFA emphasized that the interest for collaboration is mutual from the group of developed country members. But the perception is that Chinese companies are best positioned given their magnitude and cost efficiency.

[9] Danish Institute for International Studies

5.5.1 Rational Choice institutionalism (RCI)

Emergence

The RCI perspective provides a good analytical frame for understanding how China could be seen to pursue domestic interests through the AIIB. From an RCI perspective China is seeking to maximize utility through optimizing the use of capital reserves. Two points will be addressed below. Firstly, China's search for alternative investment opportunities for foreign reserves, and secondly, the promotion of Chinese industry.

The low interest rates on treasury bonds provide a natural search for alternative investment options to yield a higher return from the Chinese currency reserves. Investing in infrastructure provides the opportunity to turn foreign reserves into real assets. Another benefit is the diversification of the investment portfolio, which currently consists of mainly of U.S securities and treasury bonds (Sun, 2015). The large amount of currency reserves placed in the U.S economy, has been a growing area of concern for the Chinese leadership (Sun, 2015). The desire to address the risks associated with the strong economic ties to the U.S economy has increased the desire to diversify. Moreover, the idea to diversify currency reserves into regional infrastructure is coherent with China's "One Belt, One Road" initiative (OBOR) (Bob et al., 2015). The purpose of this initiative is to increase economic and cultural connectivity between China and Eurasia (WO-LAP, 2016). The implementation of this strategy will happen through what is termed as the Silk Road Economic Belt (SREB) and a Maritime Silk Road (MSR) (ibid). These initiatives should provide an infrastructure foundation with new opportunities for effective trade and transportation, which will increase the economic connectivity within the region. The initiative also seeks to increase economic ties with Africa and the EU. Therefore, investing currency reserves in regional infrastructure is contributing to a greater strategic move that goes beyond simply diversifying reserves and seeking higher investment yields. This can be seen as a utility maximizing move, as it is a complimentary strategy that serves a clear financial purpose and simultaneously supporting a grand economic strategy benefitting Chinese exports. This point is supported in by DIIS Senior Researcher:

"(On the emergence of AIIB) In my view it is mainly for China's economy, The Chinese economy needs a new engine of growth and you know the old way of huge investment within china and relying cheap low value added products is not sustainable anymore" (DIIS, interview material)

Now we turn to address the issue of overcapacity, which is the second point of domestic rational motivation for establishing the AIIB. China currently face an overcapacity in their economy, which is particularly large in materials-producing sectors such as steel, cement, photovoltaics, and wind power (Kawai, 2015). The domestic companies are in need of new market opportunities to continue growth. New export opportunities are essential to maximize the economic efficiency of these companies. China can boost exports through devaluating the RMB and thereby making their export more attractive. Another option is to expand export markets through strategically financing projects that create a desired demand. Given the existence of the finance gap discussed in factor 2 and a desire to invest currency reserves the latter option would serve to maximize utility. It would be evaluated to be strategically beneficial as the current economic climate makes the transaction costs for investing abroad lower than a devaluation of the currency (ibid).

The RCI perspective offers an elegant explanation of the emergence of AIIB. The institution can be seen to fulfill a demand for an institutional vehicle to implement strategic goals tackling domestic economic concerns.

Design

The inclusion of developed countries does not follow a direct rational logic if the sole purpose of the AIIB is to create a vehicle for boosting domestic exports. This suggest that the AIIB could be part of a broader strategy. One that seeks to boost Chinese influence at a global scale through closer collaboration with developed countries. Using an RCI perspective to examine the design of the bank one could question the effective power of developed countries. Regional countries control 75 percent of the shares in the AIIB, and China is likely to have more than 25 percent of the voting shares. Interestingly, China has emphasized that it will not use its effective veto rights in the AIIB (Wharton, 2015). From an RCI perspective this move signals that the opportunity cost of not including developed countries is higher than the benefits of the veto power. This is a significant move signaling that China is estimating large benefits from cooperating with developed countries. But even without the veto power the leading role of China in the AIIB is undeniable. This is emphasized by the location of the headquarter in Beijing, and the president, Jin Linqun, being a Chinese citizen. Such a design allows China to maintain a large degree of control while being conducive to collaboration. This effectively minimizes the cost of foregoing veto power. Additionally, the multilateral approach could be seen as a step to internationalize the RMB. If China is successful in increasing trade within the region, more countries will hold a larger part of their currency (Kawai, 2015). If countries hold more RMB reserves the international significance of the currency will increase.

The RCI perspective emphasizes that developed countries should be seen to accept limited direct influence, because they achieve other benefits due to their membership. This suggests that developed countries envision economic benefits by their membership. Whether this relationship of mutual benefits will materialize will be dependent on the project selection and procurement policies. The design of the policies appears to be according to international best practices. However, our interview data suggests that there is an uncertainty around the level of implementation of these policies. These considerations do suggest that many developed countries have acknowledged the benefits of building close economic relations with China. To put it in rational terms, developed countries estimate the benefits from participation will outweigh the cost of accepting China as the leading actor.

Sum up of findings using an RCI perspective on Factor 3
Emergence - The AIIB is emerging to diversify Chinese domestic reserves by allocation into growth promoting infrastructure investments - The AIIB supports Chinese strategic initiatives to increase economic and cultural connectivity within the region - The AIIB could provide a stepping stone to internationalize the RMB - Investments made by the AIIB could help create new export opportunities that could alleviate domestic overcapacity in China.
Design - China's decision to forego the veto right reflects a strategic decision to optimize developed country participation, while still maintaining control through the institutional design.

5.5.2 Historical Institutionalism

Emergence

The HI perspective argues that institutions emerge to reflect a change in power structures. The careful reader will acknowledge that the following point share similarities with the argumentation of the RCI perspective. This section will address three major points of power change. Firstly, moving the Chinese economy from mainly producing low value added products to high value added products has contributed to rethinking the use of currency reserves (Sun, 2015). Secondly, changes in the economic markets rooted in the financial crisis have caused China to look for options to diversify its currency reserves. Thirdly, the Chinese stimulation of their economy have led to the creation of an overcapacity, which cause powerful domestic companies to push for an increase of access to foreign markets.

It is acknowledged that China has evolved greatly both economically and intellectually over the past decade. The sheer magnitude of Chinese economic activity is reflected in the $3,8tn held in foreign reserves[10]. Historically the purpose of these reserves has been to control the exchange rate of the RMB, in regards to the U.S. dollar. From an HI perspective one can argue that China grew through using the exchange rate to make the Chinese currency artificially weak. From an HI perspective China created a power structure where they used their unequal position, to create an advantage in the export of low value added products. For this reason, an estimated amount of 2/3 of these reserves is held in U.S. securities and treasury bonds (Wharton, 2015). This strategy has been instrumental to China's ability to grow their production base. With China moving up the economic ladder, scholars argue that part of the motivation behind the AIIB is to take the first step towards challenging the hegemonic status of the U.S. dollar. Interestingly, this means challenging the very power structure that allowed China to give use their currency to create an export advantage. Industry experts note that the bank is expected to raise some project funding in RMB denominated bonds. Such a move can contribute to make the AIIB members hubs for RMB settlements, which will increase the international significance of the RMB.

The AIIB have been argued to be an attempt to diversify foreign currency reserves. Recent economic events have increased the justification for diversifying into infrastructure (Industry expert, interview material). The volatility in stock markets, signified by the financial crisis, and lately the domestic Chinese market crisis, has provided great concern. Additionally, the low yields on developed country securities increase the bargaining power of promoters of infrastructure investments. Infrastructure is an interesting asset as it provides an investment that is often uncorrelated with traditional market volatility (DIIS, interview material). Thus, infrastructure can be seen as a useful alternative as it allows for a decreased dependency on unpredictable markets.

[10] 2014 numbers

Moreover, this type of investments is historically embedded in the Chinese perception of stimulating economic growth.

The series of government stimulus packages implemented to boost domestic growth in China have contributed to the creation of an overcapacity with powerful Chinese companies. Given domestic demand limits and the bargaining power of domestic companies the Xi administration has made it a top priority to stimulate foreign demand (Sun, 2015). Taking the leading role in an infrastructure MDB have historically proven to increase foreign demand for exports. Thereby, the emergence of the AIIB is coherent with the path of the Chinese economy. The HI perspective allows us the freedom to use the existing economic and power structures to create an understanding of the motivation of the emergence of the AIIB.

Design

Now we move on to an analysis of the design of the institution. This section will address two points deemed central to how the design of the AIIB works as a tool for Chinese foreign policy implementation. Firstly, we will address the large number of developed country members, and how China's interest in increasing economic power is limited by existing structures. Secondly, we will address the formulation of procurement and project policies and the concerns about implementation.

China has succeeded in drawing many developed countries to the table. Most major European countries have joined, signifying the lack of action from Japan and the U.S.. This suggests that Europeans do not see China as a threat, but rather as an economic partner. The Chinese position as a leader in a multilateral finance institution is more damaging to Japan and the U.S. than to European countries. This is coherent with the existing inequalities in the international system. In the current constellation U.S. and Japan have more to lose given their leading position in the ADB (Japan & U.S.) and the World Bank (U.S.). The large number of member countries is beneficial for China to create relationships that goes beyond what currently exists. Such relationships are central to China gaining the power that comes with being embedded as an equal partner and recognized as an actor, which opinion is worth including in agenda setting. This argument is central for HI, as it shows how the members of the AIIB represent a response to the existing power structures. It needs to be noted that in order to gain international recognition the AIIB will have to operate according to accepted international standards. This limits the potential innovation of the MDB model. But interestingly, the AIIB has succeeded in some degree of design innovation in the sense that it is structured to operate faster and more efficiently than existing institutions. This is emphasized by its non-resident Board of Directors, which gives more power to the banks management. The management are not officially representing a specific country and therefore not directly infiltrated in political power struggles. Such a constellation is similar to the CAF, a Latin American MDB consisting of mainly developing country members. The CAF is renowned for its speed of operations making the choice of this structure coherent with the prioritization of operational speed. All existing MDBs with powerful developed country members have resident boards.

Moving to the analysis of the procurement and project policies the analyses of the design illuminates that the choice to become a truly multilateral institution has affected the operational policies. This is consistent with the HI perspectives emphasis on institutional isomorphism and the effect of path-dependency. A lead negotiator from the Danish MoFA emphasized that China exercised pressure to finish negotiations at an early stage. Developed countries pushed the negotiations to be prolonged with a large focus on procurement policies, project policies, and safeguards. This means that embedding an institution like the AIIB into a truly multilateral context has limited the ability of China to openly pursue the domestic agenda. The HI perspective emphasizes that an institution will have to carry a certain resemblance to existing institutions to receive an operational mandate. Therefore, China's acceptance of a limited degree of freedom in the structure of the bank could be interpreted as a pragmatic way to engage in the establishment of relationship. Additionally, the likelihood of Chinese companies winning projects are seen to be high even with transparent procurement policies. Chinese companies are very cost effective and that gives them a good chance of winning projects even in direct competition with foreign companies (Industry expert, interview material). In that sense, state of the art procurement policies could provide a platform for positive recognition without a significant loss in potential benefits to the Chinese economy. These policies could additionally contribute to expanding the operational capabilities of Chinese firm as it will increase the likelihood of collaborative relations.

Sum up of findings of using an HI perspective on Factor 3
Emergence - The AIIB is a tool to internationalize the RMB and for the currency to gain power in international markets - The AIIB can be seen as a tool to diversify the currency reserves to avoid strong dependence on the U.S. and limit exposure to volatile financial markets

- The AIIB is supporting both foreign and domestic economic agendas through solving overcapacity by expanding foreign demand
Design - The U.S. and Japan attempt to delegitimize AIIB to protect their favorable position in existing power structures - The AIIB's embeddedness in the multilateral system has pushed procurement and safeguard policies towards international standards.

5.5.3 Sociological institutionalism

Emergence

In this perspective the main motivation behind the AIIB is a domestic pressure to legitimize China as an international economic actor and to preserve a culture of growth. The authoritarian nature of the Chinese system is only legitimate as long as economic prosperity is increasing at an appropriate rate. Through collaboration with regional and developed actors China can establish legitimacy through acting according to the logic of appropriateness. Moreover, these relationships can contribute to a greater mutual understanding, which will lead to a more equal perception in trade relationships with the West. So the AIIB can be seen to emerge as a response to domestic pressures to shape relationships, which allows China to become embedded in the global financial system. The success of such behavior contributes to increase economic opportunities through growing distribution channels of high value added goods and services. Moreover, if China is perceived to be acting appropriately it will be more likely to increase its political relevance on the international scene (ODI, interview material).

Design

Two major socialization processes are notable in the design of AIIB when addressing this factor. China pursued an open approach to secure that the AIIB gained the necessary legitimacy as an organization. Thereby, China acted to fulfill cultural norms necessary to enhance the perception of Chinese companies. A key motivator for selecting an open approach is related to the desire to legitimize China and build strategic relationships with developed countries (ODI, interview material). Secondly, the developed countries have joined to secure their ability to affect the institution, and secure a degree of control through installing a set of normative ideas. One could argue that they engaged in playing the role of a gatekeeper. In the sense that they have accepted China's leading role but their presence greatly limits China's freedom of action in the implementation and formation of policies.

Sum up of findings of using an HI perspective on Factor 3
Emergence - The AIIB is an institutional response to domestic pressures for a greater embeddedness in the global financial system through the formation of legitimate relationships
Design - China's open approach is driven by cultural pressures to show a willingness to act fair and transparent. - Developed countries join to secure that the institution maintains a certain degree of appropriateness.

A List of Underlying Mechanisms

Our Stage 1 analysis is characterized by the detailed analysis of the three factors. Through applying the three perspectives of New Institutionalism we have been able to gain a more detailed understanding of the case, the AIIB. The three perspectives have allowed us to take three different approaches to the same factor, and this has uncovered a diverse set of mechanism in play. We have provided a list of the mechanisms uncovered below. The list provides a label of displaying which approach has been central in uncovering the mechanism. As seen below, there are many overlaps where two approaches have been central in uncovering a given mechanism, which is coherent with our expectation of theoretical overlaps. This notion will be addressed in greater detail below.

Table 7

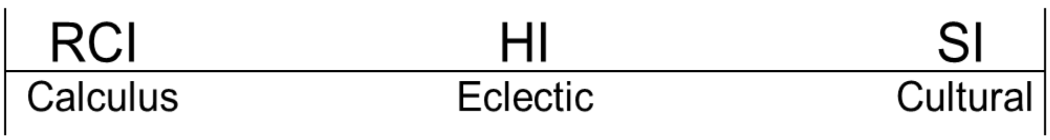
Factor	Emergence	Design
Factor 1 Uneven Representation	- The opportunity costs and a utility limitation associated with uneven representation within IFIs (RCI) - China and Asian developing countries seek to increase direct influence in regional decision making (RCI) (HI) - Economic power shifts exaggerate uneven representation and the AIIB is the institutional response (HI) - Absent historic change rooted deeply embedded power structures and path-dependency (HI) - Lack of effective reforms of existing IFIs has created legitimacy for China to materialize its own institution (SI) (HI)	- A desire to maximize utility through lowering transaction cost (RCI) - The effects of historic Chinese pragmatism (HI) - Pressure to achieve high multilateralism to be seen to act appropriately and gain institutional legitimacy in the field (SI)
Factor 2 Infrastructure Finance Gap	- A pressure to increase supply and efficiency of development finance in Asia (RCI) - A response to a decreasing infrastructure focus by existing	- A pressure to limit political and economic transaction costs (RCI) - A desire to enable more private sector

	MDBs (HI) - Changes in the North-South power balance (HI) - The legitimacy of the AIIB is obtained through managing the potential tradeoff between pragmatism and sustainability (HI) - The AIIB contributes to the socialization of China as a legitimate international actor (SI)	engagement (RCI) - The effects of Institutional Isomorphism (HI) - The diverse members could contribute to collaboration reducing the North-South divide (SI)
Factor 3 Capital Capacity	- To diversify Chinese domestic reserves by allocation into growth promoting infrastructure investments (RCI) (HI) - To support Chinese strategic initiatives and desire to increase trade in the region (RCI) - A pressure to institutionalize the RMB (RCI) (HI) - A domestic pressure to alleviate overcapacity through increasing access to new markets (RCI) (HI) - Domestic pressures for greater embeddedness in the global markets and an increased international legitimacy (SI)	- A strategic desire to collaborate with developed countries manifested by the decision to forego Veto power - The U.S. and Japanese attempts to delegitimize the AIIB to maintain power, both chose not to join (HI) - A pressure to form internationally accepted procurement and safeguard policies (HI) - Pressure to display a willingness to act fair and transparent - Collaboration as a mean to act appropriately

5.6 Interconnectedness in the Stage 1 Analysis - How the Achievement of Legitimacy Becomes a Rational Choice

As outlined in the findings from the stage 1 analysis, an interesting connection exists between the findings at each end of the theoretical continuum applied.

Figure 10



Source: Author

We have basically concluded that the reasons for why the AIIB emerges finds most explanatory power within RCI, while the reasons behind the actual design of the institution finds its strongest arguments within SI. These two combined, with the more theoretically balanced and historically rooted HI perspective, makes us arrive at a thorough and holistic analysis of the reasons why and how the AIIB emerged.

As indicated in the headline of this section, the existence of a connection between legitimacy and rational behavior is crucial in the understanding of the AIIB. Here we need to include a temporal element, with the introduction of a short and long-term perspective. The costs of achieving legitimacy around an institution, such as the AIIB, are not a rational choice in the short-term, as China can finance loans themselves (see factor 3). Our analysis interestingly has revealed the opposite when applying a long-term perspective - as China's motivation within the development field is more complex and sophisticated than the surface might reveal. A strong illustrative way to think of this connection is to see each isolated approach reaching its maximum utility much lower on the curve, than when the two are combined. This gives the pursuit of legitimacy and rational behavior the opportunity to correlate in the long-term and reach a higher maximum – one the short-term would never have achieved. The temporal dimension suggests that China has now reached a level of skill and experience within the development field that allow them to effectively align short and long-term interests. Without a SI perspective in the analysis we would have missed out on the connection between the very rational choice of pursuing legitimacy.

While HI captures the overall essence of this conclusion, we would have been left with a too simplistic understanding without the two other perspectives. They have delivered the very specific answers to this complex analysis, as they can be seen as two "extreme" perspectives. While an analysis has to be careful with conclusions based on such theoretical perspectives, it is worth emphasizing the strength derived from these polarized perspectives in regards to the AIIB. As they try to move as close to a theoretical state of a "constant" world view, one representing positivism, the other social constructivism. It naturally forces the researcher in the disciplined case study to focus the analysis on certain aspects of the case. The triad of perspectives represented in New Institutionalism therefore reassures the researcher of the dangers of diluting explanatory power by a singular HI approach, while simultaneously avoiding the extreme conclusions made from a pure RCI or SI perspective.

Our stage 1 analysis supports Hall's aforementioned advocating for a more multidisciplinary approach to the study of institutions in IPE, as the literal wording of the discipline also implies.

With these remarks the thesis continues into the stage 2 analysis of power structures through the Strangeian lens. Represented by the four pillars framework it creates a theoretical connection to a pragmatic approach to complex real world events.

6. Stage 2 Analysis – Four Pillars Framework

Referring to the second part of our research question focus is in the stage 2 analysis on answering the question ***who benefits?***

Strange emphasized how the researcher should be aware of the intertwining of the four pillars, constituting the analytical foundation of her framework. Therefore, we are fully aware of the difficulty in separating the pillars. This means it would always be possible to further discuss whether a given finding actually originates from one or another pillar. It would not be possible though, to create a systematic and structured analysis of structural power change in regards to our case, the AIIB, if we had not analyzed the four pillars separately. Our chosen approach significantly improves the ease of reading our analysis, which has been a conscious aim given the complexity of the case. Furthermore, the final conclusion of this analysis is also intended to establish a connection across the four pillars in an appropriate way. We will begin our analysis with the Money & Finance pillar, and then continues with Knowledge, Production and finally Security, before we end up with some concluding remarks.

6.1 Money & Finance

Money & Finance	This pillar is concerned with the governing of the market structure and the availability of credit. The power in this structure is dependent on the ability to control the terms on which finance is supplied.

According to Strange, the power within the Money & Finance pillar lies in the ability of providing credit - and the strength of that power can be defined as the legitimacy/credibility of the credit provider (May, 1996). With regards to structural change and the AIIB, we will discuss three main categories within the power of credit supply. Firstly, the importance of institutional legitimacy around the power to supply credit that contributes to sustainable development. Secondly, the structural impact of the entrance of the AIIB in the MDB community. Thirdly, the power to spark financial innovation that generates new sources of finance, or make more efficient use of existing ones.

Institutional Legitimacy Driving Structural Change in the Credibility of Finance

The AIIB impose a structural change by creating increased legitimacy around the ability of developing countries to actively participate in international development. The fact that China has succeeded in laying the groundwork for a multilateral institution, suggests that China is increasingly perceived as a legitimate actor. This point is supported by the participation of countries such as Denmark, Germany, the UK, and a considerable amount of other developed countries. This offers a vehicle for an incremental structural change were developing countries, through the AIIB, achieve an opportunity for a greater influence on agenda setting. It is important to emphasize that this process is likely to be incremental, as change will be dependent on a gradual integration of South-South institutions into the international system. Thereby, the AIIB becomes the first "serious" institution with a collaborative approach to institutionalizing the power of developing countries to supply credit in Asia.

The Perceived Urgency, Legitimacy, and Collective Gains

The scarcity of infrastructure finance in Asian developing countries limits the competition of supplying this type of finance. Actors are not seen to be fighting for their relevance in the market. The existing actors are acknowledging their inability to provide the magnitude of finance needed for infrastructure development. This leads to an environment where contributions from new actors are welcomed. Existing actors see an opportunity for collective gains through the entrance of new actors. An actor like the AIIB could help expand the range of possibilities for current finance providers, through providing additional capital. To apply a traditional international relations term, the structure for providing credit is not a zero sum game, as there are prospects of mutual gains through collaborating with new actors.

> *"The President of the ADB, Takehiko Nakao, and the Secretary General of the Multilateral Interim Secretariat of the AIIB, Jin Liqun, confirmed their commitment to working together for Asia and discussed future collaboration and cofinancing. The IMF, World Bank and IFC have also highlighted their willingness to work together with the AIIB to meet the infrastructure financing needs of Asia"* (Ashurst, 2015).

The vision for collaboration is currently being implemented in real project work, as three of the four projects currently being considered by the AIIB, is structured as co-financings. The project collaborations are with the EBRD, the World Bank and ADB, respectively. Hence, the AIIB is perceived as a legitimate provider of credit by existing institutions.

The AIIB is expected to drive a structural change increasing the influence of developing country credit within the region, at least in the long-term. In the short-term, the AIIB will be dependent on the abovementioned collaboration with existing institutions. Such collaboration will likely mean adopting certain practices from existing institutions, which will limit the banks initial ability to "change the game" (Elgin-Cossart & Hart, 2015). The agenda setting power of the AIIB will likely increase as other of Sino-centric institutions[11] gain more traction within the region and in the international development finance community. The importance of China in the world economy makes it inevitable that China will gain a larger influence in international infrastructure finance. To what extent the interests of other developing countries will be represented within AIIB remains to be seen, but the 75 percent voting share reserved for regional members suggests that these interests will be acknowledged.

There is a chance that power struggles could occur if the investment terms of the AIIB's credit supply become critically different from existing MDBs. Hence, this would create counterproductive behavior leading to a struggle for legitimacy among multilateral credit providers. Given the design and stated policies of the AIIB, such clashes are unlikely to become a significant factor (ODI, interview material).

The Power to Drive Financial Innovation

In analyzing the power of innovation, the AIIB is well positioned to contribute with innovative solutions to existing structures. The management and the structure of the bank is very conducive to engagement of private finance. The investment possibilities of the bank are envisioned to be more flexible and enable a more pragmatic use of bank loans, equity investments, and guarantees. This strategy is likely to allow the bank to enable more private sector engagement (Bei, 2016). Various fund structures and guarantee mechanisms are currently being discussed within the development finance community, but three major factors create difficulty in finding scalable solutions. Firstly, the limited ability of MDBs to undertake risk (ODI, interview material). Secondly, private investors, and especially institutional investors, are unable to deal with non-commercial risks and lack the expertise to effectively evaluate this type of investments (Industry expert, interview material). Lastly, there is a skepticism among borrowing countries to allow excessive private investments in key infrastructure:

> *"We know that there are multiple developing countries that have problems with having private investors involved in development practices within their countries"* (MoFA, interview material).

This is interesting, since increased private finance can potentially lead to a tradeoff for borrowing countries between immediate access to finance, and future control of central domestic functions.

[11] Referring to not just to the AIIB, but all Sino-centric institutions.

Thus, these concerns should be incorporated in future fund structures to successfully allocate the risks to those best capable of mitigate them (Ashurst, 2015). But still maintaining an acceptable level of domestic power over central infrastructure. The success of tackling these challenges will be dependent on a wide collaboration, incorporating private, public, and multilateral actors. As such, the AIIB cannot drive this change alone. However, the AIIB can contribute with an organizational structure that is designed to begin to address some of the structural issues, and could play an important role in setting the innovative agenda in the long-term.

Sum Up & Structural Change
- The AIIB drives a structural change through legitimately institutionalizing a developing country driven credit supply in the Asian region. As such, the AIIB has gained the structural power to supply credit within the MDB community.
- The change is unlikely to have a negative impact on the structural power to provide credit for current institutions. Rather it is perceived to have a possibility to increase the efficiency of the MDB community. This is possible, as there is a deficit of credit supply within the region.
- Power struggles could occur if the terms surrounding the AIIB's credit supply become critically different from existing MDBs. Hence, this would create counterproductive behavior leading to a struggle for legitimacy among multilateral credit providers. Given the design and stated policies of the AIIB, such clashes are unlikely to become a significant factor.
- The AIIB is driving an incremental change increasing the agenda setting power of regional developing countries through a large voting share in the institution.
- The progressive design of the AIIB makes it well positioned to undertake a leading role in enabling an increased role of private finance.

6.2 Knowledge

Knowledge	Actors with power in the knowledge structure are those who are in a position to determine what knowledge should be produced, and what is considered legitimate.

The knowledge pillar is a difficult pillar to define and the inclusion of this pillar has been the main cause of criticism in the application of the Strangeian theoretical framework[12]. It could be argued that knowledge is an underlying mechanism in all the pillars. For example, knowledge could be argued to affect who is likely to win contracts on projects, or contribute to a pursuit of increased

[12] See theoretical section

interregional trade to prevent conflicts. As such, the reader will need to accept an increase in the level of abstraction in this section. The arguments made on knowledge are typically two-sided, because a structural change in knowledge is often not diffused simultaneously to everyone. This is because the causality is iterative in the sense that new knowledge creates a change in behavior, which then again creates new knowledge. It is often difficult to define what drives the change in the first place. An example could be the increase of green energy projects. One could argue that the lower price of green energy technology has made it more attractive to build this type of projects. However, one could also argue that the reason green energy has become cheaper is because more knowledge has been created through a conscious choice to pursue a greener agenda. This is largely based on a scientific discovery that the use of fossil fuels has lasting damage on our environment. But this knowledge has not always been accepted, and proponents of a green agenda have long been ridiculed before certain events caused these ideas to become accepted in more general terms. The point of this argument is that knowledge is multilayered, and is closely connected with the underlying mechanisms that are so important given our critical realist focus. Sadly, these underlying mechanisms are messy, and once one decides to address them, one must accept a lack of clarity and clear causal relations. To be brief, the deeper one dives in the underlying mechanisms, one either has to be very specific or increasingly abstract. As such, generalizations are difficult. The reader must accept that the knowledge pillar relies on this premise, and does not seek to create a clear argument for a specific structural change. Instead it addresses some of the underlying mechanisms driving the knowledge behind structural change.

The purpose of the AIIB is not to create a knowledge creating institution at par with the World Bank - given the focus on creating a lean institution. The AIIB is still introducing mechanisms for changing the basis for creating knowledge in the MDB community, and this could be argued to be a structural change. Not through creating lots of new knowledge, but through legitimizing the knowledge embedded in the AIIB as an institution. The fact that the AIIB is rooted in China, introduces an institutional legitimacy around Chinese development approach. The degree of structural change is dependent on the AIIB's ability to generate acceptance around new ideas in the current system. The AIIB is not likely to achieve the power to define the platform for knowledge creation, as it is not within its institutional abilities to directly challenge the World Bank on knowledge creation. This analysis will address three areas of potential structural impact. Firstly, the knowledge institutionalized through the AIIB can help drive a positive impact on the perception of developing markets within the financial markets. Secondly, the "clash" of knowledge, or what could tentatively be termed as the Beijing vs. the Washington Consensus, is a point that needs to be addressed. Thirdly, the development of a best practice bank by drawing on existing knowledge, could allow MDBs to use resources more effectively ahead.

The Market Assessment of Developing Country Investments

A MDB that is not perceived to have the legitimate operational capabilities, will be "punished" in the markets through a correspondingly high cost of credit. Such mechanisms are not market flaws; they are quite oppositely signs that reflect the market is functioning efficiently. The cost of capital resembles the risk perceived by the market. So while this mechanism is not flawed, the effectiveness of risk premiums is dependent on the ability to precisely evaluate risks (Kahneman, 2011). Such risk perceptions are often biased, especially in context of developing countries, as data is scarcer and structures are more uncertain (Industry expert, interview material). In our interview with a private sector expert the view that the perception of developing countries risk is exaggerated was confirmed. This argument can be seen as weak as it can easily be argued to be subjective, but as noted above structural changes in knowledge might occur without an immediate effect. The argument was that the high risk perception is often due to a lack of track records, and with a lack of data the financial markets have a tendency to apply Murphy's law[13]. The emergence of the AIIB as a legitimate institution is a potential driver of a structural change through incrementally demystifying developing country infrastructure investments. The core of this argument is that the entrance of legitimate developing countries as financial actors, is going to introduce a better ability of global market actors to evaluate developing country infrastructure investments. An increased understanding of, and increased data on this type of investments, could help enable an increase in market-driven financial flows. As such, the increased understanding of these markets could have an effect on the underlying mechanisms that drive the perception of developing countries. Such a change will have multiple outcomes - one being increased financial flows and a relaxing effect on risk premiums.

The Tentative Clash of Knowledge

One could expect that the emergence of the AIIB would spur a heated debate around the Beijing and Washington Consensus, and especially the U.S. have addressed concerns around China's

[13] Anything that can go wrong will go wrong (Reference on this)

approach to development (Elgin-Cossart & Hart, 2015). However, our interview data stresses that the application of such doctrines, to clinically divide the Chinese and Western approach to development, is seen to be a simplified and mainly academic approach to the topic (ODI, interview material). Such an approach downplays the fact that decisions are more often based on a desire to find solutions for pressing problems, as opposed to be guided by strong ideological preferences. It is acknowledged that China has traditionally had a specific Chinese approach to development, which differed significantly from the Western approach. The Chinese model has a larger focus on the pragmatic pursuit of mutual benefits, opposed to the Washington Consensus, which focuses on implementing specific political reforms to spark long-term development. There is no doubt that categorizing the difference in the perception of effective development is valid to a certain degree. The negotiations around the Articles of Agreement (AoA) of the AIIB have illuminated that there are differences between how China and the Western developed countries perceive development. Our interview with a Danish lead negotiator revealed that the Chinese officials displayed great confidence in the Chinese model (MoFA, interview material). Chinese officials perceived their experience and knowledge within the field to be superior. Hence, there might be minor North-South clashes rooted in patriotic pride, but it is unlikely that such differences will amount to actual conflicts in operations (Elgin-Cossart & Hart, 2015).

The Best Practice Bank

The AIIB has deliberately attempted to create a state of the art institution through hiring some of the leading development experts to design the bank. This is emphasized by the impressive CV's of the management team and the hiring of Steven Linder[14] to design the safeguards. If the organizational model proves to be successful, it could help accelerate the reforms to improve efficiency in other MDBs. This would happen through a mutual knowledge spill-over effect through collaboration on projects. In this sense it is likely that the AIIB will learn from the operational knowledge of existing institutions. But the AIIB can contribute through its more "modern" modus operandi and this could eventually lead to the creation of new knowledge, contributing to reforms within the existing institutions. This is an attempt to improve, as opposed to challenge, the modus operandi of existing institutions, and therefore adding and not necessarily changing, the existing power structure within the Knowledge pillar.

[14] Safeguard specialist previously employed at the World Bank

As noted above the Knowledge pillar is difficult, and the structural change in this pillar is of a less visible character than in the other pillars. It has proven difficult to address specific changes, but have allowed us to address some of the more abstract implications of the emergence of AIIB. If one had to address the overarching question of ***who benefit***? it is likely to be developing countries led by China. Developing country knowledge will be more likely to be perceived legitimate through the existence of the AIIB.

Sum Up & Structural Change
- The AIIB is institutionalizing developing country experience and knowledge to allow for a better assessment of infrastructure projects in developing countries. The process is dependent on the creation of additional data and a change of perception in evaluating the risk of investing in developing country infrastructure. This is likely to be an incremental change, as it will be correlated with the improvement of developing country business environments. This creates a "chicken or the egg" type of situation, where finance will only flow once a market is perceived safe enough to accept realistic risk premiums. As such, the AIIB provides not only finance, but could also contribute to changing the systemic perceptions of developing countries.
- The US has attempted to discredit the AIIB by using negative rhetoric to address China's approach to development. An attempt has been made to install the perception of China as an illegitimate provider of credit. But the knowledge clash between the Beijing Consensus and the Washington Consensus does not seem to have much traction among experts in the field.
- If the AIIB becomes successful at materializing as a best practice MDB, it could create a push to increase the speed of reforming existing institutions through the effect of a knowledge spill-over through collaboration. As such, if the AIIB remains true to its initial strategy it could provide the foundation for structural acceptance of the knowledge contributions coming from developing countries.

6.3 Production

Production	The power here lies with the actor who has the ability to determine what type of infrastructure is produced, under what terms, and how the production and procurement process are defined.

The AIIB has provided a platform for China and regional developing countries to address their dissatisfaction about the current terms on which infrastructure is produced. As we have stated several times, the finance gap has produced a perception of urgency that have been used to justify an increased pragmatism in the approach to get infrastructure projects financed, designed, and constructed.

Depending on how you choose to view China as an actor – different scenarios will appear which will be discussed below in the analysis of the structural changes caused by changes within the production pillar.

First Scenario – Short-Term Interests Approach by China

A more pragmatic approach, in this case referring to a lowering of safeguards and a leaner and more time efficient assessment process of loan giving, would change the power structures. The AIIB is determined to align production practices more effectively with developing countries, which is a change in power structures. This change is possible, since developing countries hold a majority of the voting power which determines effective change of production practices in the bank. The AIIB has furthermore called for a larger focus on specific country plans and through the supply of various support functions assisting domestic development. This change is more than just a political agenda, as it could contribute to more effective infrastructure development and heighten the project quality and local capacity-building. Something already addressed in the bank's policy foundation:

> *"(...) the Bank stands ready, through its financings, to assist its Clients in achieving their nationally determined contributions, including through mitigation, adaptation, finance, technology transfer and capacity-building."* (Nassiry & Nakhooda, 2016).

Thinking of the design and construction of large scale infrastructure projects, a key feature about the AIIB will determine a lot – will it truly operate as a green infrastructure MDB? "Green" is in the AIIB's modus operandi, and becomes a determining factor in regards to foreseeing the ways of production. If green infrastructure will not take precedence, the structural power change will still be quite substantial. Chinese state owned enterprises (SOEs) will be positioned with some comparative advantages - since most funding comes from China, and all international institutions do take into account the donor country when awarding major contracts (UN procurement specialist, interview material). When you award contracts within international institutions, and if the project at hand is primarily or solely funded by one member country, you will most likely strongly consider a company from that member country, if it obviously fulfills all specifications in the tender.

Whether the AIIB will be green or not does not change the fact that evidence supporting the AIIB will be operating from a more pragmatic standpoint than most existing MDBs exists. In the interview with the Danish negotiator involved in the Articles of Agreements (AoA) negotiations this point was emphasized – and the same has been expressed by the bank itself (AIIB, 2016d). When the AIIB hired Steven Linder (the World Banks Safeguards guru) to formulate the safeguards policy, they tried to create a policy framework where the quality could not be contested. While at the same time strike a balance that makes it possible to get involved in projects that the existing MDBs might not be able to finance. This is the same kind of structural power change, just more elaborated and exemplified.

Second Scenario – Long-Term Interests Approach by China

In the other scenario, the AIIB will operate according to the green mantra, as multilateralism and the strong European ownership are assumed to guarantee. This perspective brings us to a rather different and interesting outcome. Large scale infrastructure projects are often awarded on the basis of a Design-Build contract approach, which means some companies design the projects, while others construct it (Amtrak, 2016; Amtrak, 2014; World Bank, 2016). If the AIIB pursues a green and sustainable infrastructure agenda, as is declared in its AoA, the competitive business landscape looks very different than the one described above. Multiple European engineering consultant companies could be expected to win the design contracts, while local (when the local business community is not too underdeveloped) or Chinese companies would win the build part of the contracts.

Seen from a structural power perspective, this would still make economic power regarding infrastructure more concentrated around China and other developing countries. The really interesting is though that it makes the "pie" bigger, which means we will see the potential of absolute gains being created. Multiple actors would benefit from the emergence of the AIIB in facilitating financing for these projects. The arguments that make this scenario rather solid stem both from the economic and political realm. The political and economic arguments are intertwined, but to clarify the points made a separated elaboration is made below.

Political Considerations

International institutions are political entities, and therefore they are often subject to more than just rational choices, as we saw in our stage 1 analysis. Should the need for green expertise not be the reason behind awarding European companies contracts, there would still be a political desire to do so for particularly two reasons, 1) legitimacy and 2) political tensions between Asian countries. The first reason was strongly emphasized in the interview with the aforementioned Danish AIIB negotiator:

> *"(...) the Chinese will certainly be aware of the political aspects of awarding contracts to companies, especially politically important companies. I mean companies that originate from member countries with political capital, either because of the economic strength or because of the more symbolic signals. Political symbols are absolutely a huge part of this game and China's inviting in to build credibility around the AIIB. That's for sure."* (MoFA, interview material)

But there is also another very interesting political aspect of getting specific members to join the AIIB. China needs neutral actors to get involved in the actual production of infrastructure, otherwise these projects can easily get jeopardized by regional tensions. Here the case with Chinese SOEs in Indonesia serves as a prime example of this concern (which also might be the reason for Indonesia to join the AIIB rather late) (ODI, interview material). This aspect was further emphasized through interviews with Procurement Officers from the UN, who described how difficult it can be to initiate essential infrastructure projects if the contracting company is from a politically "sensitive" country (UN procurement specialist, interview material). Here Denmark has a strategic advantage by having world class infrastructure companies and being a neutral political actor in Asian regional disputes – obviously a motivational factor behind Denmark's membership, which leads to the economic aspects of the argument.

Economic Considerations

Regarding green infrastructure, it can be argued that the lack of expertise forces China to let European companies bid on projects as their expertise would be the enabling factor in making these projects economically successful – especially in the long-term as mistakes are costly. Furthermore, another obvious motivation for China to invite the European companies to the "party" is that Chinese SOEs inevitably will benefit from knowledge transfer processes. This will position them more competitively in future projects not just in Asia. Again, there is constantly a juggling of short and long-term interest and a desire to make them correlate, as was also a finding in the stage 1 analysis. China is not the only actor pursuing an active agenda though, as European countries also have a huge economic incentive in securing influence within an institution well positioned to create economic returns for European companies. The European economy is suffering from low growth rates, which creates both economic and political incentives to contribute to structural power changes with the production pillar.

Sum Up & Structural Change
- Structural power changes will occur within the production pillar both in a short and long-term perspective independently of the nature of infrastructure.
- Given that China is the primary architect and capital subscriber behind the AIIB, Chinese companies are expected have a significant competitive advantage in winning contracts – mostly traditional infrastructure projects.
- Political and economic considerations behind the emergence of the AIIB will benefit European companies when infrastructure projects are rooted in sustainable and green practices, while the Chinese have the potential to reap essential know-how for long-term use.

6.4 Security

Security	The power in this pillar lies within the ability to determine the agenda and the arena in which security concerns are tackled. Security structures are often seen to be affected by pressures from the three other structures.

Analyzing potential structural power changes within the security pillar will be done by separating into domestic and foreign threats. The choice of doing so stems from a conviction that it is helpful to clarify whether a threat originates within an actor, or is a consequence of the actions of other actors, as that is essential for understanding the nature of structural power changes.

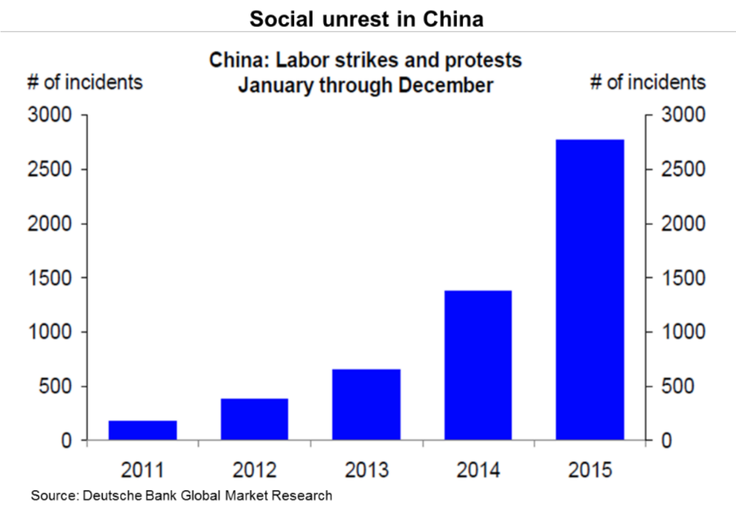
It is important to keep in mind that security structures are much affected by pressure from the three other pillars. It can basically be argued that the mere emergence of the AIIB, and other Sino-centric institutions, are proof of a structural power change. The AIIB has already been successful in fueling discourses that have been left out according to developing countries (ODI, interview material). Most evidently is our factor 2, the infrastructure finance gap in Asia, a strong example of an issue getting substantial attention. The reason why we analyze this within this pillar is because it has direct security implications. In our analysis, some issues originate from a domestic decision, but evolve into a threat due to foreign involvement, therefore the separation will sometimes be relative. Let us begin with the domestic threats.

Domestic Threats

Lack of access to infrastructure finance is a growing security threat among many developing countries in Asia (ODI, interview material). To use the Strangeian terminology, it is a lack of security supply, which means the establishment is incapable of providing the effective means to secure its population. The potential threats range from pollution, lack of energy supply, basic health, to poverty, insufficient access to clean water, and food. Moreover, lacking sufficient infrastructure will limit the possible development trajectory of a country, leaving the population in a vulnerable situation in a globalized world where many threats are truly global by nature.

In a Strangian analysis of power change the allocation of risks and the associated costs are centrally positioned, which can be exemplified with the following. Firstly, the AIIB is an arena created to combat the risks associated with lack of infrastructure financing. Furthermore, it is a way to minimize the costs that will inevitably follow from not fully succeeding in this endeavor. The AIIB is in this case not intended to reallocate, but simply to eliminate risks. The second example is pursuing real investable assets suitable for allocation of capital reserves, as the risks of financial markets have huge potential costs (factor 3). This one is caused by the actions of foreign actors, actually the accumulated actions of all actors, China included. Volatility in financial markets becomes a domestic threat when it has the potential to destabilize the economy and create social unrest – something Beijing is fully aware of. Labor Union demonstrations have dramatically increased the last couple of years, which creates increased political risks in China.

Figure 11



Costs are in the second example, two-fold. 1) The cost of satisfying the short-term politically motivated needs, and 2) the opportunity cost of capital, which comes from holding capital that could have been invested in higher yielding assets – in this case, infrastructure. In the creation of investable long-term assets addressing security threats, developing countries benefit the most from the emergence of the AIIB.

Another domestic security issue worth mentioning is the connection between high growth rates and a political stable climate in China (see above). This link suggests a more general observation relevant across pillars, which is the nature of the Chinese growth model. The model seems incredibly adaptable in a pragmatic way to its environment (Communist political system with a market economy), as long as the output is sustained growth. This means that as minimal disruption as possible is in China's interest, as long as growth rates are acceptable – pragmatism above ideology. If you imagine security and growth rates as the two curves in a supply and demand diagram, China is then constantly trying to position itself in an equilibrium. Only when the equilibrium is shifting and growth is suffering, China is willing to risk disruption and therefore security, to regain growth as it is pivotal for long-term success according to the political rule.

Foreign Threats

As mentioned above, many of China's concerns revolve around domestic security issues, as well as the ability to sustain high growth rates – and looking at foreign threats, the goal is no different. One of the things that make our case so interesting to study is its infant phase and therefore continuous evolvement. Very recently the bank proposed its first four projects:

- **Indonesia:** National Slum Upgrading Project (Co-financed with the World Bank) - 06/01/2016
- **Bangladesh:** Distribution System Upgrade and Expansion Project - 05/16/2016
- **Tajikistan:** Dushanbe-Uzbekistan Border Road Improvement Project (Co-financed with the European Bank for Reconstruction and Development) - 04/26/2016
- **Pakistan:** National Motorway M-4 (Shorkot-Khanewal Section) Project (Co-financed with the Asian Development Bank) 05/09/2016

(AIIB, 2016e)

The last two projects are of great interest from a Strangian perspective for the following reasons. Firstly, the projects are directly related to securing transportation, which is one of Strange's sub-pillars in her structural power framework. Secondly, it can be argued that the two projects are directly aligned with the Chinese President, Xi Jinping's *One Belt, One Road* initiative, also called the *Silk Road Initiative*. This initiative is a strategic move by China to make trade more independent from the countries controlling the majority of the sea routes relevant for Chinese trade. As many of these countries have close ties to the U.S., China is eager to limit dependency on these relations. This is needed from a Chinese perspective, as these relations constitute a greater foreign threat than those in the Caucasus region (Bergsager, 2012). The AIIB becomes a tool for redefining China's most important trade routes, thereby changing the balance of power within the region. But it is not just China who benefits from this change. Thirdly, the Tajikistan project is also beneficial for Russian interests, as they benefit from increased economic activity in their region.

Another foreign threat we have chosen to highlight is the tradeoff many developing countries are faced with between getting much needed capital and getting the desired providers of this capital. Looking ahead, there exists broad consensus in the development finance community that private capital will become more and more important (Senior Executive at the World Bank, interview material). Private capital in vital infrastructure could lead to a loss of control of central domestic functions (MoFA, interview material). Concerns are also directed towards foreign sovereign capital, which raises new national security concerns. Loosing sovereignty and becoming subject to the interests of foreign actors are definitely concerns among many developing countries, as it impairs the borrowing states ability to take vital action necessary to uphold the security of its population.

Sum Up & Structural Change
- The AIIB has the potential to mitigate domestic security threat within developing countries, and particularly in the Chinese case by sustaining growth rates important for the political establishment.
- The AIIB can re-alter the structural power in regards to trade routes by enforcing the importance of new, which limit the dependency on the existing routes embedded in previous power structures. This changes the landscape of foreign threats.
- The inability to finance sufficient infrastructure impair a government's ability to provide basic security for its population. Furthermore, accepting external finance from private investors or sovereign states can also affect the capacity to provide security.

6.5 Concluding Remarks – Stage 2 Analysis

The key finding from our stage 1 analysis again appears in this stage, focused on structural power shifts. As the first scenario depicted in the production pillar showed how massive Chinese dominance would create a structural power change - it might not be a sustainable one. To create real structural power shifts as a rising power, legitimacy is a key feature. This was the essence in the Money & Finance pillar. Displayed in the second scenario within the production pillar, we saw how the foundation for a legitimate change is actually present. This is the consequence of multiple actors in the development field, both existing and rising powers, benefiting from the emergence of the AIIB. It is impossible not to include the implications for the U.S. in an analysis of who benefits from the AIIB. The U.S., currently the most powerful actor in this field, has actually lost quite substantial power so far. Obstructions made in regards to concerns about environmental impact, procurement processes, and governance transparency surrounding the AIIB, has so far proved less significant – as major allies such as the UK, Germany, France, Denmark, Switzerland, and Australia has chosen to become founding members of the bank. What is worth emphasizing is the nature of the concerns directed towards the AIIB – all referring to legitimacy.

So far, China has been very successful in navigating attention away from these concerns, as they have been tapping into particularly two broadly recognized discourses. These two discourses emerged from two of the three factors know from stage I. 1) The existence of an infrastructure finance gap, and 2) uneven representation. This momentum has been used to create institutions for structural power changes. Another crucial point to stress is how the AIIB as an institution is capable of generating more than relative gains. This gives the Europeans much needed new economic options in a time of economic growth stagnation and political dissatisfaction with the establishment. The figure below displays China's significance as a global growth engine. This increases the incentives for European countries to increase economic relations with China.

Figure 12

China has wisely pursued multilateralism at this time, and therefore, created the preconditions by the AIIB to legitimize their stepping up the latter within the development field. In addition, other new Sino-centric institutions create the foundation of long-term growth, which will further bring structural power change.

To directly answer the part of our research question ***who benefits?*** in relation to China, the answer is: Not just China, but China is the only actor who benefits from the structural power changes across all four pillars. This consists more specifically of the following:

- **Money & Finance:** With the AIIB, China becomes a legitimate financial development supplier.
- **Knowledge:** The Chinese approach to development becomes institutionalized in a multilateral body, capable of incrementally increase legitimacy around this approach.
- **Production:** Chinese SOEs will be well-positioned to win large scale infrastructure contracts and over time acquire and develop knowledge currently concentrated in European companies.
- **Security:** Capital allocation into new assets facilitated by the AIIB will have the potential to stabilize the Chinese economy and make it less depended upon volatility in the market and the U.S. economy. Furthermore, the AIIB can re-alter the regional trade routes by strategic infrastructure investments favorable from a Chinese security perspective.

7. Discussing of Private Capital Barriers

In this part of the thesis we will discuss some key barriers for private capital that we identified throughout our research process. In addition, the role of the private sector in society and economic systems will be discussed.

2015 was undeniably one of the most interesting years in international development and development finance. The year included multiple successful negotiations that led to ambitious frameworks and commitments for future actions. We will briefly touch on three major events that deserve to be mentioned to understand the motives driving international development:

- The third international conference on Financing for Development held on 13th-16th of July 2015 in Addis Ababa, amounting into the Addis Ababa Action Agenda.
- The adoption of the Sustainable Development Goals on 25th of September 2015. These are 17 goals guiding the future of international development practices. They replace the Millennium Development Goals and seek to engage a broader array of actors in contributing to global development.
- The COP21 conference in Paris achieved a more ambitious commitment to combating climate change. Including a set of Intended Nationally Defined Contributions allowing countries to define their own commitments.

The conference in Addis Ababa deserves a few additional comments, as it specifically addressed the daunting tasks of establishing the financial foundation for reaching the Sustainable Development Goals (UN outcome document, 2015). The outcome of this conference was the Addis Ababa Action Agenda consisting of the following:

- Gathering domestic public resources
- Increase the engagement of domestic and international private business and finance
- Increase the international development cooperation. This includes increased South-South cooperation and the use of public finance to enable an increase of private investments.
- Continuously use trade as a growth engine and push for greater use of technology and science to increase development effectiveness through innovation.
- Address debt and debt sustainability
- Lastly, address systemic issues (UN Outcome Document, 2015).

The list in itself is not revolutionary, but according to a Danish government official attending the conference, the interesting take-away was how the engagement of the private sector had progressed from previous conferences (MoFA, interview material). Interestingly, the follow up conference happened in April 2016. The talks here specifically addressed how to use MDBs more effectively as enablers of private finance in infrastructure investments (UN Outcome document, 2016). To sum up, the task for development finance is becoming even larger as ambitions are raised.

Major Market Barriers for Private Capital – Obvious and Less-obvious

Again, the complexity of the interconnected issues in the development finance field amazes us as our iterative process continues. As a web of issues has revealed itself throughout the research we have chosen to focus on the following three major barriers for private capital to be invested in developing countries; 1) project development and pipeline, 2) complexity of current guarantee system, and 3) paradigmatic discrepancies between professions. All three barriers got confirmed several times during the research process from different communities, which has been the reason behind the selection.

Existence of a Market - Project Development and Pipeline

Maybe the most obvious market barrier in this field is that the fundamentals of an actual market are not established. There are two main reasons for this, 1) project development in many developing countries are below what institutional investors can accept to allocate money into, even though they see great opportunities in the idea of the project (Employee at pension fund, interview material), and 2) lack of an investable project pipeline (Actis, interview material). The two are connected as the first has to be in order, before the other can be solved.

Competences in the field are currently scarce[15], and those existing are either fully occupied in their home markets (European Energy[16]) or just not willing to take upon the risks of developing projects in risky developing countries – which also often happens to be the ones most in need of projects.

If we accept that the conditions for a market do exist, the next barrier becomes presenting the investors with the projects that are already ready for investments. The Canadian government recently launched a platform called Convergence in an attempt to bring public and private investors together (Government of Canada, 2016). It is the first platform of its kind and the idea is to make co-investing in developing countries easier through blended financing mechanisms. Convergence

[15] We only identified one globally operating PE fund that was specialized in developing countries projects, named Actis.

[16] Specialized renewable energy project developer.

highlights the leadership role that Canada has taken to raise awareness and promote tangible blended financing mechanisms that can help address critical investment gaps, particularly in infrastructure. The quote by the Canadian Minster of International Development, Marie-Claude Bibeau, emphasizes what increasingly reach the political agenda around the world:

> *"Canada is committed to becoming a leader in innovative approaches to financing for development. Canada's support of Convergence exemplifies this commitment given that the platform will mobilize private-sector resources and expertise to help the world's poorest and most vulnerable people, which will be a crucial factor in achieving the United Nations' Sustainable Development Goals."* (ibid).

By launching this platform, the idea is a one-entry-point for infrastructure projects, which was welcomed by the institutional investors we interviewed.

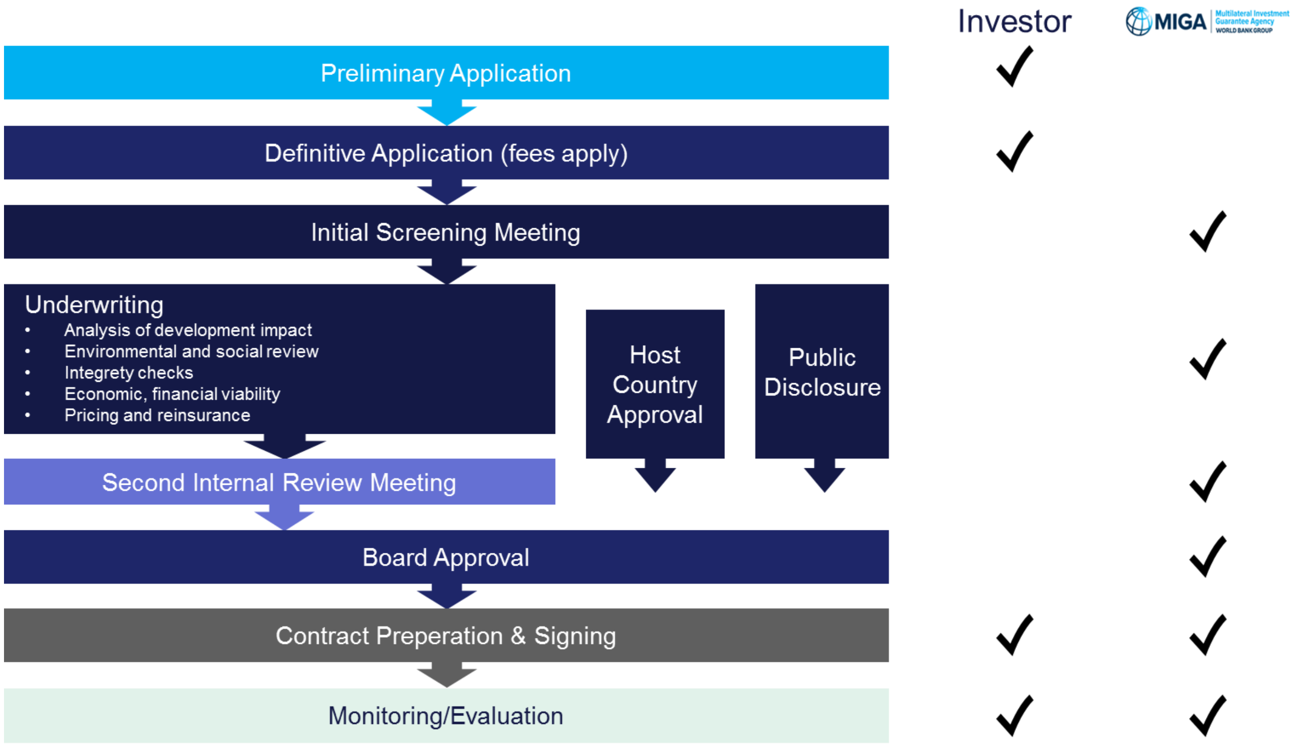
7.1 The Complexity of the Current Guarantee System

Investment risks are for good reasons one of the barriers that has received most attention in the debate around private capital involvement in infrastructure projects in developing countries. The guarantees most often applied are credit, political risk, and breach of contract cover. In our interviews with the private sector, represented by a pension fund and a Public Private Partnership (PPP) fund with investments in developing countries, the current possibilities for guarantees was characterized as complex, costly, and time consuming. A Vice President from a PPP fund advocated for a much more simple system with resemblance to a basic insurance structure – everyone pay, everyone benefit (VP, PPP fund, interview material).

Even in developed markets, navigating different kinds of guarantee instruments, particularly credit guarantees, is often a huge challenge for investors and not a straight-forwards process. It is desire by investors as it creates a competitive advantage in the market. Looking at infrastructure investments in developing countries guarantees is not just desired, but often a premise, as such projects can result in social upheavals or political disagreements (Heep, 2016). The aforementioned VP from a PPP fund reported that guarantees are crucial, because even having a President signing a power purchasing agreement (PPA) in a developing country is no guarantee for long-term investments (VP, PPP fund, interview material).

In the figure below we have displayed the guarantee application process within the Multilateral Investment Guarantee Agency (MIGA), which is part of the World Bank. It is in the underwriting process where the complex and heavy load of work is allocated, and the process many investors would like to be less complex – obviously with respect to the complex nature of investing in complex markets.

Figure 13



An initiative worth mentioning in this context is the African Risk Capacity (ARC), which is a treaty-based organization established by the African Union (AU). Consisting of 41 African states it is seen as a groundbreaking project designed to manage risks from droughts across the continent. The ARC is an African-owned continent-wide index-based weather insurance pool, to secure contingency funds for drought events by capitalizing on the natural diversification of weather risk (Swiss Re, 2013; African Risk Capacity, 2016).

By creating a risk pool individual risks are transferred and combined into one. The risk profile of the pool, rather than the risk profile of each individual country, then makes the uncertainty of individual risks become a calculable risk for the group. By calculating the probability that a certain event will occur in one year, and the likelihood that droughts will happen in multiple other countries in the same year, it is possible to determine the payouts for the entire pool and therefore the funds required (Swiss Re, 2013). The idea has similarities with what our private sector respondents asked for, and therefore this initiative deserves more attention in the development finance community.

The biggest obstacle for the ARC is to function as indented is the size of the fund, which currently has a cap of USD 30.000 (ODI, interview material).

7.2 Paradigmatic discrepancies – clash of professions

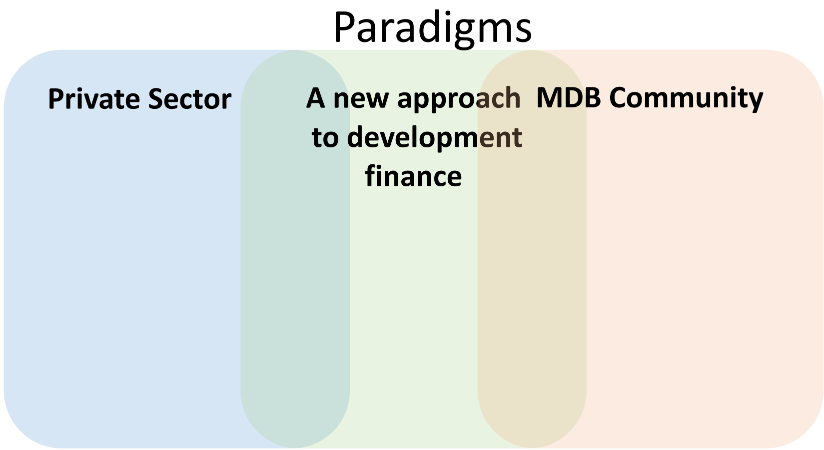
The next barrier partly relates to the first, as it concerns the prerequisites to make investments in new asset classes in new markets. To collect information and then asses it based on qualified knowledge, is here the issues. More specifically, information concerns awareness of projects and the possibilities in the market that currently exists, while the knowledge barrier can be argued to stem from more of a paradigmatic discrepancy between professions involved in facilitating a change. Emphases will here be on the knowledge issue as information was addressed within the first barrier.

The institutional investors we interviewed all expressed difficulties in accessing information about investable projects presented to them. Particularly one pension fund emphasized that difficulties of evaluating infrastructure, renewable energy, and climate related investments was primarily rooted in the lack of previous experience and expertise among the responsible Portfolio Managers:

> *"You cannot expect that all PM's at pension funds nowadays suddenly to have the expertise to assess complex projects in markets they are not familiar with, but that doesn't make it less of an issue when you look at what our members are increasingly asking of us to invest in (…) We need change that is for sure, especially when it comes to increased diversity in the skills set of employees. I think many are starting to realize that."* (Industry expert, interview material).

One aspect of the knowledge barrier relates to the skills in-house at institutional investors, another is the paradigmatic discrepancies between professions, which is more sophisticated and complex to resolve.

Figure 14



Source: Author

As MDBs have been identified to be the most suited facilitators of private capital flows into developing countries, they need to develop in a way sometimes forgotten in the debate. Looking at employees at MDBs, it is rather the rule than the exception that you hold a Ph.D. in Developmental Economics (Former employee at regional MDB, interview material). There are obviously good reasons for having employees with the skills that follows from a Ph.D. within this field, but as the operating environment of MDBs are changing, so has the composition of employees. Furthermore, it is not just a question of skill-sets, but just as much a question of the use of terminology and the broader spectrum of possible interpretations. Much of the barriers preventing fruitful cooperation between institutional investors and MDBs are rooted in misconceptions, miscommunication, and a lack of financial instruments attractive for the private capital (ODI, interview material; industry expert, interview material). During an interview with a Danish pension fund we were presented with this issue illustrated by the case of the International Development Association (IDA), part of the World Bank Group. IDA reached out to the fund for a meeting to present their products, but the fund simply refused to take the meeting as they felt that IDA did not understand their perspective and mandate – and this is one of the most proactive pension funds in regards to alternative investments in energy, infrastructure, and climate related assets (Employee at pension fund, interview material).

From all the interviews across the three communities (policy, private sector, and academia) we end up concluding that striking an equilibrium where skills and mindsets cross over between the two categorize of professions would probably leave us with the most extra value added. It is probably not as simple as hiring more MBA graduates at MDBs and hiring more diverse portfolio managers at institutional investors, but it might be an easy first step towards increased interdisciplinarity within both professions.

7.2.1 On the Right Trajectory?

One could ask whether patience is now what we need to see all the new initiatives to materialize? It is a difficult question, but in an interview with Lord Nicolas Stern, former Chief Economist at the World Bank, he referred to a recent study that covered the needs for sustainable infrastructure. The paper concluded that all infrastructure build from now on, has to be *sustainable* if we are to achieve the goals decided upon at the COP21. Currently that is not the case (Interview material). The professor is interestingly also a member of the AIIB's Advisory Board.

7.3. The Increasing Significance of Private Finance and MDBs as Market Making Actors

It is largely established in the literature that a significant increase in private capital is necessary to provide a realistic plan to achieve the multitude of goals within sustainable development (Reisen, 2015; Humphrey, 2015). To revisit the writings of Strange, she expressed a deep criticism of the large role the private sector has in the developed world (Strange, 1997). She perceived the sectors to be unconstrained and self-governing. To Strange the behavior of the private sector resembled gambling, and it was incapable of providing the necessary governance for a sustainable market (Strange, 1997). Strange was largely concerned with the skewness in the state-market nexus (Strange, 1998). She would advise for great caution if the private sector where to be allowed to own public infrastructure. However, the undeniable need for private sector investment in infrastructure is creating a paradox between Strange's pragmatism and her distrust in the private sector.

At the other side of the spectrum there is a large academic strand arguing for the benefits of privatization (Sheshinski & López-Calva, 2003). The arguments include increased efficiency in all aspects of the development process, and the potential for a fast development of an efficient financial market due to privatization (Mathur & Marcelin, 2015). There is no doubt around the validity of the academic strand that argues for the effectiveness of the private sector. Moreover, there are multiple indicators towards that private sector incentives are increasingly becoming aligned with inclusive growth. In our research we found that Danish pension funds are faced with increased pressure from their clients to invest assets categorized as socially responsible investments (Employee at pension fund, interview material). Other studies show that companies that operate with a focus on environmental and social impact actually perform better and are therefore also monetarily better investments (Industry expert, interview material). Sadly, this trend is still largely confined to a small number of companies and countries. In our research it has become clear that there still exist unaligned incentive structures between short-term profit maximization and effective development (MoFA, interview material). Add to this paradox the intertwined incentives of the international community, and the complexity becomes almost overwhelming.

The privatization of traditional state tasks in an international system begs the question as *"who has the power to set the agenda for the governance of such a market?"* and *"how do you govern the incentives?*". Strange argued that as markets are increasingly privatized the division of labor between private and public become increasingly blurry, but simultaneously such a division becomes more important than ever. The circumstances under which market structures evolve are central to maintaining the control that would allow for a satisfactory alignment of incentives. Here David Bull (2010) argues that the multilateral system is able to undertake such a task:

> "*The multilateral system coordinates relations not only between states but also between private for-profit and non-profit organizations"* (Bull, 2010: 185). He continues to argue that the current system is favorable to market forces:
> *"The current form of multilateralism is set out to support the global capitalist system rather than challenge it, and initiatives that make use of business methods and market mechanisms will have a greater chance of succeeding than those that do not"* (Bull, 2010: 185).

This underlines the importance of the MDBs, as they are the institutions designed with the capabilities to be the connection between the public and private actors. In our analysis it is shown that MDBs are very political organizations so it is undeniable that MDBs serve a political purpose. This point should hardly be surprising at this stage of the thesis. It becomes increasingly important when it is connected to the idea of uneven representation. This implies that states can have the ability to use MDBs to align public and private interests with domestic agendas – if they are the ones benefiting from the skewed representation. This power to pursue domestic agendas through MDBs is by no means a new thing, but it is amplified as private actors become more involved and as development finance moves further away from being controlled by states. As such, MDBs gain a larger responsibility in defining the market structures. Hereby, power in the MDBs could become increasingly important to the formulation of agendas and very important for both private and public interests. The point is not that MDBs will be solely responsible for the establishment of an increasingly structured development infrastructure market, as this would be an overstatement. The point is that as private finance gain significance, the channels for government control moves towards multinational institutions. Controlling the supply of infrastructure could prove very powerful. On a positive note our findings suggest that China is entering with a desire to increase collaboration in the field.

Addressing Other Theoretical Contributions within the Field

Before concluding we will briefly broaden the discussion and briefly address how our findings align with other theoretical perspectives of institutionalism and international development. The following is not intended to introduce any new arguments our contributions. The purpose is rather to briefly explore how our findings align with other theoretical approaches to the study of institutions and economic development. We will discuss how different economic visions (China and the West) could impact existing institutions in the future. The following section will discuss the significance of our findings in the light of Varieties of Capitalism (VoC) (Hall & Soskice, 2001), which is an important theoretical strand within the study of institutions.

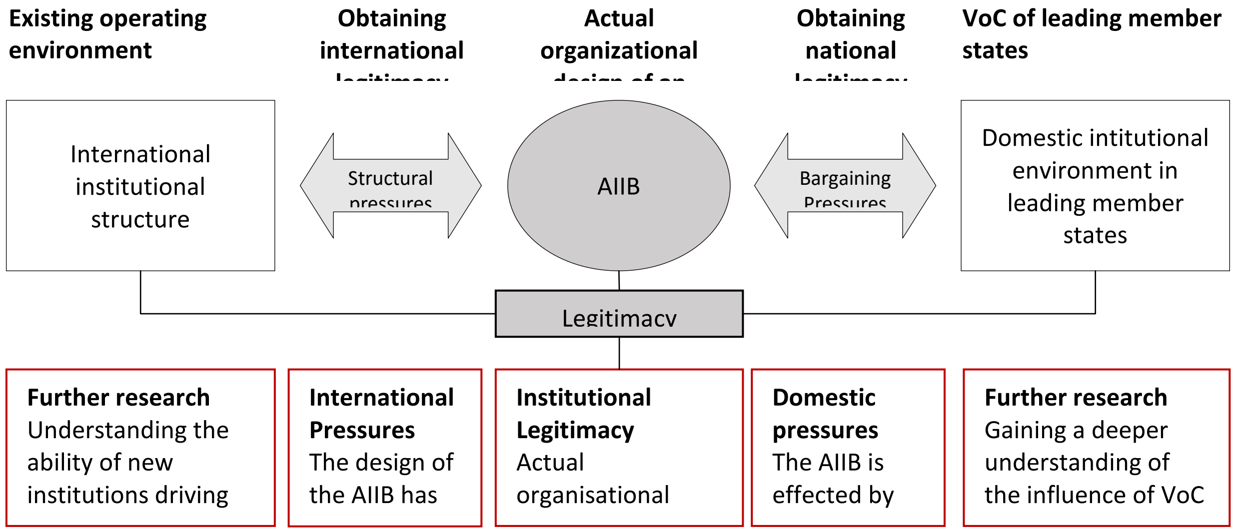
Varieties of Capitalism and MDBs

The political changes enforced by MDBs have often carried traces from their domestic economic ideologies. Given the institutional focus of this thesis, it seems appropriate to address the VoC framework as a frame for potential further research. The VoC framework is interesting to discuss, as it can be used to gain a deeper understanding of how domestic institutional systems influence international institutions. A greater understanding of how the domestic system affects international behavior could increase the understanding of what drives a given action in the international forum.

The VoC framework was originally developed to systemize the systemic differences in developed countries. This framework has been used in many comparative studies to understand how the obvious differences affect various types of organizations in different systems. An academic branch of this literature has examined the effects of how domestic institutional constellations among members affect the design and operational practices of multinational enterprises (MNE) (Hull & Morgan, 2006). To clarify, an MNE originating from a liberal market economy (LME) or a coordinated market economy has been found to be likely to carry trades of their respective domestic systems. This study becomes interesting when thinking of MDBs, as this thesis demonstrates how the AIIB is affected by its Chinese architects. A similar effect of important member countries can be seen when examining the World Bank and the ADB. These connections become increasingly interesting, as developing countries with vastly different systems become more powerful in development. Hence, a study focused at understanding how the VoC of powerful countries within an MDB affect the operating practices, would be useful to gain a better understanding of the potential trajectories of new institutions.

The analytical findings of this thesis suggest that the quest for legitimacy is central to the institutional design of an MDB. In that sense, an MDB led by China will still largely be designed to comply with existing international institutions. This means that an MDB is facing two major external institutional pressures. On one side, the systemic pressures to obtain legitimacy in the international system. On the other, domestic institutional pressures from the powerful countries within the organization affects the institutional design. So in a VoC perspective the AIIB will be affected by pressures from influential member states, which will obviously primarily be China, but there is no doubt that other member states will have influence too. This is displayed in the following figure:

Figure 15



Source: Author

Three major points of interesting further research arise from these observations. Firstly, to what degree does the VoC of central member countries affect the institutional design, and what are the powerful channels to affect this design. Secondly, to gain a more sophisticated understanding of the connection between a certain operational design and legitimacy. Thirdly, how actors can change the very foundation upon which legitimacy is based would be a future area of interest.

As such, a deeper understanding of the influence of national institutional structures and international structures could provide a better understanding of how the MDBs are used as a political and economic tool. Finally, we turn to briefly discuss of our findings in the context of the debate of a decoupling between the business cycles of developed and emerging markets[17] before concluding (Akin 2012).

Decoupling vs. Recoupling

A body of academic work has evolved suggesting a decoupling of business cycles between developed and emerging markets led by the BRICS countries (Godement, 2012). It is argument that strong trade regimes between the BRICS countries lead to the creation of a decreased dependence on trade with the developed countries. One could argue that the emergence of new BRICS institutions, such as the AIIB and the NDB could be an institutionalization of a separation of the developed and the emerging markets.

A further look implies that this does not seem to be the case. Of the four projects that have been revealed by the AIIB, two could be argued to have a strong connection to the One Belt One Road initiative[18]. Moreover, China's explicit intension to collaborate with existing institutions does not indicate any decoupling pressures related to the AIIB. The collaborative intensions are reflected in the majority of co-financings in the announced projects. Given our findings and the opinions of experts interviewed, this is an attempt to increase the developing country involvement in the MDB system rather than an attempt to create a new system of emerging and developing market actors (ODI, interview material). It needs to be noted that for further research on this topic, the NDB tends to be seen as a much more political project and potentially an attempt to institutionalize the ties between the BRICS. Therefore, we suggest that this institution is a more suitable case for a study directed towards institutional decoupling.

8. Conclusion

[17] Concentrated around the BRICS, which is why the term developing countries is avoided.
[18] See case presentation.

What are some of the key factors that led to the emergence of the AIIB, and what role did these factors play in the emergence and design of the AIIB? Who benefits from the AIIB, and what are the key barriers for private capital in development finance?

In answering the research question we conducted a two-stage analysis and a discussion. The first part of our research question was answered in the stage I analysis, where we applied the different New Institutionalist perspectives of RCI, HI, and SI to the three key factors identified. The factors were identified by applying the following selection criteria: 1) the phenomenon is described by experts as having a significant impact on the emergence of the AIIB, 2) the emergence of the AIIB has an impact on the phenomenon - changing its nature, and 3) there is a consensus around the phenomenon in the field. This lead to these three factors:

1. Uneven Representation
2. Infrastructure Finance Gap
3. Capital Capacity

Applying the New Institutionalist theoretical perspectives to these factors proved very useful in the disciplined interpretive case study, were we sought to uncover some of the underlying mechanisms in the process of the emergence and design of the AIIB.

Factor	Emergence	Design
Factor 1 Uneven Representation	- The opportunity costs and a utility limitation associated with uneven representation within IFIs (RCI) - China and Asian developing countries seek to increase direct influence in regional decision making (RCI) (HI) - Economic power shifts exaggerate uneven representation and the AIIB is the institutional response (HI) - Absent historic change rooted deeply embedded power structures and path-dependency (HI) - Lack of effective reforms of existing IFIs has created legitimacy for China to materialize its own institution (SI) (HI)	- A desire to maximize utility through lowering transaction cost (RCI) - The effects of historic Chinese pragmatism (HI) - Pressure to achieve high multilateralism to be seen to act appropriately and gain institutional legitimacy in the field (SI)
Factor 2 Infrastructure Finance Gap	- A pressure to increase supply and efficiency of development finance in Asia (RCI) - A response to a decreasing infrastructure focus by existing MDBs (HI) - Changes in the North-South power balance (HI) - The legitimacy of the AIIB is obtained through managing the potential tradeoff between pragmatism and sustainability (HI)	- A pressure to limit political and economic transaction costs (RCI) - A desire to enable more private sector engagement (RCI) - The effects of Institutional Isomorphism (HI) - The diverse members could contribute to collaboration reducing the North-South divide (SI)

	- The AIIB contributes to the socialization of China as a legitimate international actor (SI)	
Factor 3 Capital Capacity	- To diversify Chinese domestic reserves by allocation into growth promoting infrastructure investments (RCI) (HI) - To support Chinese strategic initiatives and desire to increase trade in the region (RCI) - A pressure to institutionalize the RMB (RCI) (HI) - A domestic pressure to alleviate overcapacity through increasing access to new markets (RCI) (HI) - Domestic pressures for greater embeddedness in the global markets and an increased international legitimacy (SI)	- A strategic desire to collaborate with developed countries manifested by the decision to forego Veto power - The U.S. and Japanese attempts to delegitimize the AIIB to maintain power, both chose not to join (HI) - A pressure to form internationally accepted procurement and safeguard policies (HI) - Pressure to display a willingness to act fair and transparent - Collaboration as a mean to act appropriately

Our stage I analysis also revealed how the pursuit for legitimacy within development finance can be a very rational choice by an actor. It might not be a utility maximizing short-term decision, but given the nature of development finance, being perceived as a legitimate actor is crucial in unlocking the economic potential within this field – a massive potential looking ahead. Without the SI perspective to force the researcher’s attention towards the implications of legitimacy, emphasis on this specific finding could have been missed.

Below we have displayed our findings from the stage II analysis, where we applied the Strangeian four pillars framework to analyze structural power changes and thereby answering who benefits from the AIIB.

Pillars	Who Benefits?
Money & Finance	- The AIIB legitimately institutionalize developing country credit supply, thereby increasing developing country power. - The change is unlikely to negatively affect current institutions, as an increase in finance is expected to provide collective gains. - Power struggles can occur if the AIIB undertakes vastly different policies from existing institutions – this is seen to be unlikely. - The AIIB benefit Asian developing countries through driving an incrementally increase in their agenda setting power. - The design of the AIIB will be beneficial for private actors wishing to collaborate with MDBs on infrastructure investments.
Knowledge	- The AIIB will contribute to demystify Asian developing countries and drive more efficient market practices. - The Washington vs. Beijing consensus clash seems to be largely an academic discussion with no

	real traction within the field. The U.S.'s failed attempt to introduce this clash suggests a shift of power towards China. - The AIIB can provide a vehicle to increase the economic legitimacy of China and Asian developing countries at an international scale.
Production	- Chinese companies are expected to benefit as they are seen to be in an advantageous position in regards to win projects. - Increased relationships between developing Asia countries and the EU will be expected to be mutually beneficial. It is expected to provide a much need engine of growth for European companies, and create a change for Asian countries to increase their economic internationalization and grow their knowledge pool within infrastructure.
Security	- The AIIB can contribute positively to mitigate the security threats presented by Chinese stagnation. - Improving the regional connectivity is in line with the One Belt and One Road initiative, which will lower the dependency on existing trade routes. This will make China less dependent on foreign relations with other Asian countries and increase their economic independence. - Increased private owner of central infrastructure could pose a security threat for developing countries.
General	- China is the only actor benefitting across all four pillars. - Asian developing and developed country members are expected to benefit through increased economic relations and an ability to promote domestic companies internationally. - The U.S. and Japan are the only actors seen to potentially loose, but the loss is not likely to be significant in the short-term, due to the interest in collaboration expressed by the AIIB.

One finding worth emphasizing again is that China is the only actor benefitting from the AIIB across all pillars.

Finally, through our interviews we identified three key barriers for private capital into developing countries. Firstly, the perceived lack of investable infrastructure projects, which is due to poor project development and a lack of a long-term pipeline of projects. Secondly, complexity within the current guarantee system calls for the creation of simpler guarantee system. Institutional investors and PPP funds would have a larger appetite for investments in developing countries, if various guarantees were easier to evaluate and apply for. Thirdly, we found that paradigmatic discrepancies between the MDB community and private investors create barriers. The professions are faced with a knowledge and discursive discrepancy that negatively impact cooperation and innovation of investable instruments.

In the very end of our thesis we suggested topics for further research and tried to comment on other some implications of the emergence of the AIIB that was not covered in our two-stage analysis.

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10. Appendix

Expanded description of management (AIIB):
President
Mr. Jin Liqun

- Elected as President for a five-year term. Prior to becoming president, he served as the secretary general for the Multilateral Interim Secretary, tasked with doing groundwork for creating the bank.
- Mr. Jin was Chairman of China International Capital Corporation Limited, China's first joint-venture investment bank. From 2008 to 2013, he served as Chairman of the Supervisory Board, China Investment Corporation (CIC). From 2009 to 2012, Mr. Jin served first as Deputy Chairman, and subsequently as Chairman of the International Forum of Sovereign Wealth Funds (IFSWF).
- From 2003 to 2008, Mr. Jin was Vice President, and then Ranking Vice President, of the Asian Development Bank (ADB), in charge of programs for South, Central and West Asia, and private sector operations.
- Mr. Jin joined the Ministry of Finance in 1980, where he served as Director General and Assistant Minister, and became Vice Minister in 1998. He was also a Member of the State Monetary Policy Committee. Earlier in his career, Mr. Jin served as Alternative Executive

Director for China at the World Bank and at the Global Environment Facility as well as Alternative Governor for China at the ADB.

- Mr. Jin holds an M. A. degree in English Literature from Beijing Institute of Foreign Languages (now Beijing Foreign Studies University). He was also a Hubert Humphrey Fellow in the Economics Graduate Program at Boston University from 1987 to 1988. He is a national of the People's Republic of China.

Vice President and Corporate Secretary

<u>Sir Danny Alexander</u>

- was one of the founders and leaders of the first UK coalition government since World War II.
- Sir Danny has over 20 years of professional experience.
- From 2010-2015 he served as Chief Secretary to the UK Treasury, where he secured more than £100 billion of public expenditure savings. He has played an active role in driving international cooperation on tax, trade and transparency during the UK G8 presidency.
- A seasoned negotiator and communicator, Sir Danny has engaged with diverse stakeholders and partners on key public policies.
- He led the work on UK infrastructure policy and delivery, leading to the first National Infrastructure Plan which is now embedded as an annual process.
- He helped to establish the Green Investment Bank in the UK and to develop and implement the UK Guarantee Scheme for infrastructure.

Vice President and Chief Risk Officer

<u>Dr. Kyttack Hong</u>

- Previously served the Chairman and CEO of the Korea Development Bank (KDB). In this capacity he led the merger of KDB, KDB Financial Group (which he previously led as Chairman/CEO) and the Korea Finance Corporation into a consolidated KDB to reflect the evolving financial landscape. In this process he oversaw the organizational restructuring and human resources management, working with employees and management of the three institutions to improve organizational capacity and effectiveness.
- An economist and finance expert, Dr. Hong has had a career spanning over 30 years of public service and extensive experience as an outside director for a number of financial institutions, including the Korea Securities Depository, Samsung Credit Card Company, Tongyang Securities Company. Dr. Hong served as Professor and Dean of the School of

Politics and Economics at Chung-Ang University and Managing Editor of the Journal of Economic Development.

Vice President and Chief Investment Officer

Dr. D. J. Pandian

- Has had an extensive career spanning 30 years with the Indian Administrative Services, holding key positions at the State, National, and International levels in the energy (oil and gas, power, renewable), infrastructure, finance, and industry sectors.
- Dr. Pandian was instrumental in liberalizing the policy regime to attract international investment to crucial infrastructure sectors including power, airlines, ports and telecoms.
- During his career, he has served in the Government of Gujarat in various capacities including: Chief Secretary; Additional Chief Secretary, Industries and Mines; and Principle Secretary, Energy and Petrochemicals Department.
- Dr. Pandian established the Gujarat Energy Research and Management Institute and has served as chairman, director and trustee with a number of state-owned enterprises.

Vice President - Policy and Strategy

Dr. Joachim von Amsberg

- Previously served as Vice President, Development Finance at the World Bank where he was responsible for the replenishment and stewardship of the International Development Association (IDA), the World Bank's fund for the poorest, and for trust fund and partnership operations.
- As Vice President for Operations Policy and Country Services, Dr. von Amsberg oversaw the World Bank's results agenda with its increased focus on achieving, measuring and communicating operational results and introduced the Program-for-Results lending product. He was responsible for the Bank's operational risk functions including policies on procurement, financial management, social and environmental safeguards.
- He also oversaw the Bank's modernization and reform agenda. During his 25 years at the World Bank he served as Country Director for Indonesia and the Philippines where he spearheaded the preparation of the country strategy partnerships together with the Governments and stakeholders, and managed the World Bank operational portfolios and analytical work programs.
- Dr. von Amsberg has authored a number of World Bank research reports and other publications.

Vice President and Chief Administration Officer

Dr. Luky Eko Wuryanto

- Has served in senior positions in the Indonesian government for 20 years, most recently as Deputy Coordinating Minister for Infrastructure Acceleration and Regional Development, Coordinating Ministry for Economic Affairs.
- Under his leadership, the Committee for Acceleration of priority Infrastructure Delivery (KKPIP) oversaw and coordinated the implementation of 225 National Strategic Projects totaling over US$100 billion and 22 priority projects totaling US$85 billion.
- During his career, Dr. Wuryanto has honed his strong organizational, administrative, execution and management expertise working on projects in the ports, roads, transport, energy , electricity, water and sanitation and public housing sectors.
- He played a key role in reaching consensus on the financing structure of many mega infrastructure projects in Indonesia.

Interview guides:

Interview Guide, Academia	
1	What do you see as 3-5 main reasons for the emergence of the AIIB?
2	What do you see as the main criteria of success for the AIIB?
3	How is the general perception of AIIB in academia?
4	Does the emergence of the AIIB represent the beginning of a new era in development finance?
5	Do you give any merit to the concept of a Beijing consensus and do you see a decoupling of development finance between North and South?
6	To what degree do you see the AIIB as a rational response to the (insert factor here) we have presented?
7	To what degree do you see the AIIB as a response to the existing power structures in regards to (Insert factor here)?
8	To what degree do you see the AIIB as a response to cultural and social pressures driven by (insert factor)
9	How do you see the emergence of AIIB to affect power structures on the following levels; states, Institutions, and private sector?

10	What do you see as the main barriers for private investments in infrastructure in Asian developing countries?
11	What type of products do you think the MDBs can offer that will be attractive to the private sector?

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Interview Guide, Policy	
1	What do you see as 3-5 main reasons for the emergence of the AIIB?
2	What do you see as the main criteria for success for the AIIB?
3	How is the AIIB perceived in your area of the policy community?
4	How does the emergence of the AIIB raise debate about an imminent change of the practices of multilateral development banks?
5	Is the concept of a Beijing consensus and a Washington addressed in your daily work?
6	To what degree do you see the AIIB as a rational response to the (insert factor here) we have presented?
7	To what degree do you see the AIIB as a response to the existing power structures in regards to (Insert factor here)?
8	To what degree do you see the AIIB as a response to cultural and social pressures driven by (insert factor)
9	How do you view the possibilities increasing the engagement of the private sector? What arguments does the private sector provide for their lack of engagement?
10	How do developing country officials view private ownership of central domestic infrastructure?

11	Do you see a bigger impact of multilateral institutions in future decision making?

Interview Guide, Private sector	
1	What do you see as 3-5 main reasons for the emergence of the AIIB?
2	What do you see as the main criteria for success for the AIIB?
3	How is the AIIB perceived in your area of the private sector?
4	How does the emergence of the AIIB raise debate about an imminent change of the practices of multilateral development banks?
5	Is the concept of a Beijing consensus and a Washington considered to be a factor in the private sector?
6	To what degree do you see the AIIB as a rational response to the (insert factor here) we have presented?
7	To what degree do you see the AIIB as a response to the existing power structures in regards to (Insert factor here)?
8	To what degree do you see the AIIB as a response to cultural and social pressures driven by (insert factor)
9	How do you view the possibilities increasing the engagement of the private sector? What arguments does the public sector provide for their lack of effective policies?
10	How do you view non-commercial risk? Which type of insurance mechanisms do you see to be suitable and feasible for implementation?
11	From your perspective what role would be suitable for MDBs in enabling private finance? And what type of financial products do you see to be necessary?

Selected interview:

Chris Humphrey
Guest lecturer at University of Zurich and Research Associate at Overseas Development Institute (ODI).

Bio:

Chris Humphrey is a specialist in development finance, with a focus on analyzing how multilateral development banks are adapting to an evolving world economy. Chris has worked in lending operations and research at the World Bank and African Development Bank in numerous countries in Latin America, Africa and central Europe. He has a PhD from the London School of Economics and is a researcher/guest lecturer at the University of Zurich, Switzerland.

Interview:

Julian: Hi Chris, its Julian and Jens here. Thank you for taking your time to speak with us, it's much appreciated.

Chris: No problem, I hope I'm of use.

Julian: I'm sure you will be, we already read all of your article within this field, so we are sure you will be of great use. You are quite a knowledgeable guy, so sure you'll have some valuable inputs for us.

Chris: Okay, you guys are writing a thesis together or how is this working?

Julian: In Denmark we have the opportunity to write it together, so we are a team here.

Jens: Hi Chris, its Jens here. We are currently in Wesport Connecticut.

Chris: Oh, I grew up in Darien.

Julian: We just went through there yesterday when we took the train.

Chris: What are you guys doing there?

Julian: We are living at a friend's place and then we are preparing for the Financing for Development conference next week, the follow-up on the Addis Adaba last year. Hopefully we will get in touch with a few interesting people there.

Chris: Sounds good.

Jens: Chris, if we could start, as you heard, our focus is on the emergence of the new multilateral development banks, particularly the AIIB we think is interesting as the BRICS Bank, the NDB, has potentially become a little too politicized in the beginning of it.

Chris: That's sort of my opinion of it, but yeah, we will see what plays out in reality.

Jens: But could you outline the 3-4 main reasons for the emergence of the development of these banks right now?

Chris: Are you asking exactly what about these development bank that has made them emerge?

Julian: Sort of what motivations you see from the BRICS's countries to found these banks and what goes into that? The main reasons?

Chris: Sure, uhh, obviously this is just purely my speculations I don't have any solid basis for saying this, you know, any evidence to back this up, just so that is clear. Uhhmm, I mean at the one hand there is a huge unhappiness with the way the major multilateral banks that already exists, and have been existing for a number of year, have been operating. A lot of dissatisfaction with, uhm, this is something I've spent a lot of time during research on, the know the World Bank and the major regional multilateral banks, noteably the Inter-American Development Bank, the Asian Development Bank, and the African Development Bank, a little bit less perhaps, are controlled through their voting rules by a fairly small group of major industrialized countries.

Jens: Right.

Chris: And rather than see those banks as cooperatives, where everyone works together and the borrowers are just as important as the non-borrowers, the way the cooperatives have functioned the industrialized countries has felt very entitled to be able to ramp through policies that suit their particular interests. Over the wishes of the borrowing countries, and that have been played out in many different ways. I don't know if you have seen any of my other work, but I have looked at some of these issues, specifically environmental and social safeguards, which I just published a piece on two days ago. You know, this is just one example, but it is basically right countries imposing their views on borrowing countries. With environmental and social safeguards the overall goal is trying to safe vulnerable communities etc., but what they are basically doing is imposing rules above the national laws. So they say, you might have your own laws to deal with these issues, but when you take loans from us, you have to follow these rules and forget about your own laws. And that sort of thing is highly objectionable to a lot of borrowing countries - they think it's not acceptable. That's not how a cooperative should be working and that plays out in many different areas. The kind of sectors where the banks make loans, it plays out in the length of time to get loans approved. It takes incredibly long because of all the these rules put in place by the non-borrowing countries.

Julian: Right.

Chris: It plays out in loan pricing, all sorts of issues. And because of the way the voting rules are structured in these banks, you probably know, there is really nothing that can be done about it from a borrowing country perspective. The non-borrowers have all the votes they need. They don't have the majority, but enough to control changes to the capital structure in these banks, so every times there is a need for an capital increase the non-borrowers get together and say, we are not going to give you this increase unless you accept all these impositions on the way the bank should be run.

So that's very frustrating for a lot of these banks I think. Especially China, which feels it should be able to raise its voting power in these banks. China would like to be able to contribute more to these banks by an increase in its capital share, and thereby an increase in its voting share. But the other countries have not allowed to do so.

There was a vote and voice reform at the World Bank, at the IMF as well which have been much more politicized, I'm sure you know, but at the World Bank there has been some changes, China has increased its share somewhat but if you look at the voting shares, it's a bit ridiculous that China has half the voting share of Japan.

Julian & Jens: Yeah.

Chris: Even though its economy is considerably bigger. And there is no law out there which says, you know, your voting share has to be exactly proportional to your proportion of the world economy. These are cooperative banks, a club basically, they can set the rules anyway they want, but its clearly an imbalance that China feels that should be rectified. And this is played out also especially in the area of infrastructure, because a lot of these environmental and social safeguards, rules put in place by the World Bank especially by the Pelosi Amendment, Nacy Pelosi pushed it though the US Congress, and some other rules, well, basically they haven't funded a hydropower dam in I don't know how long!

Nor have they been able to fund much of the coal fired power plants. Say what you will about the environmental impact of these, and I'm not making any judgment on that, but developing countries really need electric power. And they are not able to get that. And if it takes three years, and you have to negotiated all sorts of resettlement issues and indigenous communities and what have you, you know, then countries say, we really don't want to deal with that, we can't deal with that, we need to get the money quickly and get these projects going. **And so the banks are losing relevance in these areas.** And that is sort of above and beyond the issues of imposing policies through adjustment loans and where there is basically a set of policies a country have to follow if they want to get the money. Another issue. The way they have been running these banks have basically been objectionable, and then about a year ago the BRICS countries had enough, and they had pretty substantial foreign currency reserves, China specially had 4 trillion, its dropping dramatically, but they still have somewhere around three trillion in foreign currency reserves. And what do they do with those reserves? They put them mainly in sovereign bonds of Western countries, Germany, United States, and so they think, I imagine they think, why not take a chunk of that money and capitalize a bank. Because once they put the capital in the bank it doesn't require budgetary allocations each year, that the beauty of MDBs, generally speaking, once they are capitalized they run themselves, they are self-funding institutions. And so I imagine that China felt lets go ahead and use a little chuck of our money and do that.

The broader issue of geopolitics, and China trying to stick their thumb in the US's eye, or what have you, I don't know, this is not an issue I know a lot about, I focus mainly on the development banks themselves. But yeah, I mean, that's the main issues that I see as a motivation for setting up these banks.

Julian: Nice, in terms of you were talking about the safeguards, do you see it at sort of realistic that the AIIB is gonna become better than the World Bank and the other institutions since they have sort of a commitment from all of these western countries. They are probably going to demand at least a very high standard?

Chris: yeah, that's a very interesting question, and that remains to be seen. I've had some discussions with officials in European governments that are members of the AIIB, and it sounds like it's a very delicate dance going right there now. The thing is that the US isn't in, and the fact that the US isn't in, allows some flexibility because when these issues come up the US and the other existing banks has been very loud and dictatorial, basically insisted on no deviations and strengthening the safeguards and all the rest. Not allowing any moves to country systems, which have been attempted over the recent years. But the fact that the US isn't in there with the AIIB allows things to be a little more flexible and China has come out right away and said, we gonna be very good about this, they hired Steven Lindner, who was the World Banks safeguards guru for many years, to design their safeguards. From what I've seen of draft policy documents so far, I think they will use more of a country systems approach. I don't know whether you are familiar with that, but I think you can probably imagine.

Both: yeah.

Chris: Using country rules when possible, but where the red lines going be is going to be a little bit fussier. The red lines with the United State are very clear. With the European nations, just to give you one example, I know some folks in one of the country governments here who said, that they (the Europeans) had pushed to make the AIIB say, that they would not fund goal fired power plants. And basically China said: No. We are going to fund goal fired power plants. And the Europeans backed off, so that's an interesting debate right there, that the Europeans decided that they couldn't push that far. So I think its going to be decided on a bit of a case by case basis. I think the fact that, that there is not going to be a sitting Board of executive directors, where they are sitting there in an office in Beijing, or in the case of the New Development Bank in Shanghai, on a daily basis reviving every loan, I think that's also going to change the dynamic on the way they assert their views on the way the banks are run. Its going to be a non-sitting board, that's going to meet 3-4 time a year to decided on bigger policy issues. In the AIIB the president is going to have a lot more authority on approving loans on his own. It's a he at the moment. But at the same time, they don't want to be clobbered by NGO's around the world saying they are doing awful things. So I think they are going to be cautious, but I thinks is going to be a bit more, perhaps not as far as the CAF,

Julian: Yeah, I guess you could say that they are very famous for the speed of operations.

Chris: Yes, and other ways, but definitely speed, and also other ways where they are more flexible in their dealings with borrower countries, because they are run by borrower countries. Which obviously changes their attitude very much. And they were famous for years for just pawing the jungle, and they got a lot of criticism for that, but now they have instituted a certain set of rules, but its not just these blanked policies that covers every country everywhere. Instead they look at it on a case by case basis – there is a lot of criticism on what these judgments are made on still, and probably legitimate criticism also, but I think that’s probably the directions that the AIIB is going to move in.

Julian: Do you think it (the AIIB) will be different in regards to also be a knowledge creating bank?

Chris: No, I think they will be the same, certainly in the early years, they have been very clear about having a very lean staff, and very low budget overhead and low administrative costs. And that means they are not going to be able to hire all these people, that are going to be need for that.

Jens: Right.

Chris: So I don’t think they are going to do that. I’ve been sort of pushing both the AIIB and the NDB in my small commentaries in my blog, that if they were to become knowledge banks, they should be extremely focused, and create specific knowledge, especially on infrastructure and structuring financial packages through private sector and offering the technical assistance, the practical technical assistance the countries need on how to set up this sorts of deals. And also perhaps the engineering side of it, but very focused on infrastructure. I think that would give them a great niche, where they can develop real comparative advantage in terms of knowledge. But whether they are going to do that I don’t know. But being the expert on health, education, etc. everything under the sun – no. I’m convinced they are not going to do that.

Jens: Chris, how to you see Chinas involvement in the current MDBs, now that they have their own, do you see that they are going to withdraw a bit from the World Bank and other institutions?

Chris: I doubt it, I mean, there is no need for them to because they already paid in their shareholding capital. So they are going to have representatives there and they will still make their points there. I think China is very pragmatic unlike the other four BRICS frankly (*a little laugh*), which I think is much more politicized, no I think China is, you know the old Moa saying, I think it was Mao, let a thousand flowers bloom. You know, trying different thinks. So they are not going to give up on the World Bank, there is no need to, no incentive to I would say. And in fact what they done more recently, which is quite interesting, they put up a lot of co-financing arrangements at the IFC, the African Development Bank, Asian Development Bank, Inter-American Development Bank, I think they are also setting one up at the EBRD, and what these are, are basically pick pocks of money, a couple of billion dollars per bank – a lot of money. And what that money does it sits there and when whatever development bank wants to set up a loan, they come to the Chinese representative for this fund and say: Hey are you interested in putting your money in this witness loan, and they say yes or no. So what this functions as is basically a poor substitute for being able to increase their own capital in these banks. It's giving the banks more capital. But China doesn't get more voting power with it, but I think because these big pocks of money is there the administration of these banks they take China into account, and I think they will start taking in loan projects that they think will be more interesting to China, so they can tap these funds for these project. So I think it is an informal way of building influence in these banks, so I don't think they will withdraw at all. I think they will keep going, China I think will even expand to the smaller sub-regional banks, China has joined a bank in Africa called the PTA Bank, which I wouldn't be surprised of if you never heard of, I haven't heard of it either until a couple of years ago, but its kind of a mini CAF in southern Africa and its growing pretty rapidly and China joined on as a shareholder a few years back and I bet they will continue to do that with other smaller sub-regional banks, of which there are many in the world, there is something like 20 MDBs out there so.

Julian: Do you see, to a certain extent, a sort of a Beijing Consensus emerging as opposed to the Washington Consensus, so a clash of development paradigms, in the sense that there are two ways of thinking about development, and could these new banks be seen as instruments to create more legitimacy around what would be called a Beijing Consensus – is it a made up discussion or is there something to that?

Chris: I think it's a bit more of a made up discussion to be honest, I don't think China thinks in those terms, I think they are very pragmatic, like I say for example, Chinas is coming around to see the need and paying attention to social and environmental issues in their projects also in their China EpIm Bank and the China Development Bank, which are massive institutions by the way. They see what happens, all the issues with labor rights and all these problems with bringing in all these Chinese workers, so they are trying to change the way they do that. They had a couple of high profile blow-ups so far as I have been told, I haven't looked into them myself, but I've been told that there has been some major environmental problems with some projects. They often said through their bilateral agencies, that they have had no interest in debt sustainability, they have said forget about that, let the World Bank and the IMF deal with that, at least that's what they have done in the past – we are just gonna focus on the projects. But now they are starting to get a little weird about being paid back, so they are getting more attention to debt sustainability, which is one of these, classic, if you will, Washington Consensus, which I also think is a bit of an overblown, way of dealing with things. I think these things have been dealt with much more organically over the years depending on the current needs, but I think they are evolving pretty rapidly. I think there might have been an initial feeling that they could reinvent the wheel, but they are running up against the same issues that all the other banks have and are running up against, I mean, the World Bank began for many many years ago basically just fund infrastructure projects, that's what it did, and it didn't pay any attention to environmental and social safeguards either and it didn't look at the policy framework either and they ran into the problems that came along with that. It might have gone too far in the other direction, there are certainly arguments that can be made for that, but there was reasons why these things changed, it wasn't just some imposed ideology coming out of the US Treasury department, the US certainly had a lot of influence and acting according to its own interest, definitely, but there are real reasons for why these practice things change, and I think China is well aware of that and is willing to adapt and change as needed.

Julian: In terms of you said there were some possibilities regarding institutional investors and private finance, what type of mechanisms do you see that needs to be made and what type of financial instruments do you see to be key in realizing that more of this type of financing is needed?

Chris: Really interesting question and a huge question. Something the MDBs have been struggling with and haven't quite figured out how to deal with, because as you can imagine in this low interest rate environment, especially in Europe and the US, but around most of the world, there is a huge desire to find higher returns, and there is massive needs for infrastructure investments in the developing world which could potentially pay high returns. But yeah, I think I mentioned in my email, the institutional investors are not able to handle those risks so the MDBs are rather well positioned to do that, but they haven't found the right instruments to do that. One key instrument would be the use of their guarantees, and that's been really problematic for a number of reasons. I co-authored a paper with someone here from the ODI, were we look at some of these problems, and the MDBs have really not been able to deal with that, but it would be a great area for them to do it. But also to create co-finance funds with institutional investors, I'm not an expert in this field, haven't done an MBA myself, but it seems like there should be some potential. And I think part of the problem is that the World Bank and the big Regional MDBs are stacked with development economists and basically public sector oriented folks, because that have been the orientation of those banks. So I think there are some cultural issues there, corporate culture issues, and lack of knowledge, they don't have the experts, you know IFC, it's the one that really done the best, and EBRD with a 80% private sector focus. And the European Investment Bank as well, they are much more able to structure more complex financial products, talk the language of private investors, and make the sort of deals that can channel that kind of money. At the moment the way this is happening through the big public sector MDBs, are basically the institutional investors buying their bonds. Which is a very useful channel, but there could be more direct involvement for sure.

Julian: From the Danish II we talked with, there is definitely the interest, but it also have to be a structured product for them to buy, because they cannot do anything themselves.

Chris: Exactly, they want a nice and convenient product for them to buy. And one that can be traded and there is a liquid marked for. And they don't have anything at the moment compared to MDB bonds, which are wonderful instruments, but you cant buy them because they are so popular at the secondary market. There was this effort on behalf of the World Bank to set up this infrastructure facility, that was going to be sort of a spin off from the World Bank with some capital and really be a dealmaker, but instead it was cubed down to be a technical assistance small facility without any meaningful size. The African Development Bank spun off this thing called Africa 50, which I have a lot of doubt about, but we will see, basically it's the outgoing President Caparougo's baby, and he is actually now become the leading of it I think, since he left the African Development Bank. But it's been a lot of talk, and they try to make governments, especially central banks, to give them a lot of money. It needs to be capitalized, which I don't think they been successful with so far, as far as I know. But both of these ideas are responds to the inability of the existing MDBs to do this, which is to me, the ones that should be doing this, we should have a need for someone else to do so, a separate vehicle. But maybe the AIIB will be able to do so, at least I believe they have a better chance than the NDB because of its politicized nature. But we'll see, the AIIB is also starting with public lending because they need to create creditability in the capital markets.

Julian: Definitely interesting for them to develop these capabilities, as we have heard a lot from the Danish institutions we have talked with, that a huge part of the problem is that the developing countries don't have the capabilities to develop good projects. So it could be interesting to have someone like the AIIB to be the facilitators of projects and then some type of private actor to help develop and combine their expertise.

Chris: No question about it, and not just the expertise, and sort of the scale, but also two other things, putting some skin in the game themselves I think would make a difference, when they put up some money on themselves, which would add some creditability, but also the government to government link, that a big deal, this really helps mitigate risk because these banks are preferred creditors, so they have an informal status. But its real, you see it in loan repayment among the existing MDBs, and I suspect the AIIB to develop a similar preferred creditor status which creates a lot of comfort for private investors, because they know the AIIB can call up the President or the Finance Minister and make sure that these projects are moving smoothly in a way a private institutional investor might not be able to do themselves.

Jens: Chris, from your perspective based on academia, forums and elsewhere were you have been discussing this stuff, who other experts would you recommend having a talk with, particularly in regard to the AIIB and the role that institution can play ahead?

Chris: You can try to get in touch with a gentlemen by the name Amar B (have send him mail), I have worked with him and he is with the Brookings Institute in Washington, he brought me into this stuff. He is a little hard to pin down, because he is all over the place, but a very smart guy. Say hi.

Kevin Gallager. Boston University.

To be honest, most academics actually don’t know how these banks work, so they stay focused at the sort of broader picture, and it seems like you guys are a little more interested in the business side of things, which I’m also interested in.

Table 1. Overview of MDBs

	MDB	Type of Financing	Type of Borrower/Client	Year Founded	Members
	Established Institutions				
	World Bank Group				
	International Bank for Reconstruction and Development (IBRD)	Non-concessional loans and loan guarantees	Primarily middle-income governments, also some creditworthy low-income countries	1944	188
	International Development Association (IDA)	Concessional loans and grants	Low-income governments	1960	173
	International Finance Corporation (IFC)	Non-concessional loans, equity investments, and loan guarantees	Private sector firms in middle- and low-income countries	1956	184
	Multilateral Investment Guarantee Agency (MIGA*)	Non-commercial guarantees	Investors and lenders	1988	181
	IMF**	Provide loans in balance of payments crisis. Non-concessional and concessional. (Ref1)		1945	188
	African Development Bank (AfDB)	Non-concessional loans, equity investments, and loan guarantees	Regional private sector firms, middle-income governments and some creditworthy low-income governments	1963	80
	African Development Fund (AfDF)	Concessional loans and grants	Low-income government in the region	1972	80
	Asian Development Bank (AsDB)	Non-concessional loans, equity inv	Regional private sector firms, middle-income governments and some creditworthy low-income governments	1966	67
	Asian Development Fund (AsDF)	Concessional loans and grants	Low-income government in the region	1973	
	European Bank for Reconstruction and Development (EBRD)	Non-concessional loans, equity investments, and loan guarantees	Focus on private sector firms and developing country governements in the region	1991	64
	Inter-American Development Bank (IDB)	Non-concessional loans and loan guarantees	Regional private sector firms, middle-income governments and some creditworthy low-income governments	1959	48
	Fund for Special Operations (FSO)	Concessional loans	Low-income governments in the region	1959	
The MFIs differ from the MDBs in that they have a narrower ownership/membership structure and they focus on special sectors or activities	**Multilateral Financial Institutions (MFI) (Ref3)**				
	The European Investment Bank (ref4)	Project loans, intermediated loans, venture capital, microfinance, equity and fund investments and various blended products as guarantees as the most relevant for our focus.	Public and private entities, member states and areas of interest to member states	1958	28
	International Fund for Agricultural Development (ref5)	Concessional loans and grants	Developing country member states to finance poverty elevation projects	1977	176 member states
	The Islamic Development Bank (ref6 and 7)	Equity capital, grant loans, leasing, Special funds for specific purposes, trust funds, and various Shariah-compliant financial products.	Public and private entities within member countries	1973	56
	The Nordic Investment Bank (ref 8)	Loans, project and structured finance through funds and PPP. Guarantees	Primarily corporate loans to member countries, but also direct loans to member governments and municipalities.	1975	8
	Nordic Development Fund (ref 9)	Previously concessional loans, now only grants	Low-income countries	1989	5
	The OPEC Fund for International Development	Concessional loans and grants	Least developed countries. Primarily for private sector activities	1976	13
	Sub-Regional Banks (Ref3)				
	Development Bank of Latin America (Ref 10)	Grants, medium and long-term loans, credit lines, equity investments, syndicated loans, guarantees, and trade finance.	Public and private sector (banks and companies)	1970	19
	Caribbean Development Bank	Loans	Regional member countries. Non-regional members not allowed to borrow	1969	28
	Central American Bank for Economic Integration (Ref 10)	Loans, co-financing, syndicated loans, guarantees, credit lines, working capital	Public financial and corporate private sector	1960	13