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The New Development Bank (NDB) vs The Asian Infrastructure Investment Bank (AIIB): An analytical comparison from a critical perspective

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Abstract

The NDB and the AIID are two important recent milestones of multilateral cooperation aiming at reducing the financial gap in infrastructure development in the Global South. They were established thanks to the strong initiatives of prominent Southern leaders, BRICS for the former and China for the latter. These institutions present many institutional and operational similarities as well as differences. This paper traces the respective diplomatic background that led to their establishment; compares and contrasts their characteristics as envisaged in their respective Articles of Agreement as well as observed in their early institutional development and lending activities; and contemplates likely outlooks of their activities and their effects on international political economy. Some of our key points are as follows. The new institutions, at least during next several years, are not likely to induce large impacts on infrastructure financing (a few billion dollars a year). The NDB may thrive to be as pro-development as a South-South institution could be. The AIIB, however, may have to compromise in this regard due to the sizeable and increasing participation of Northern donors. Yet, neither of them is likely to grow to be alternatives to the existing multilateral financial institutions. We foresee that the NDB's membership, institutional building, and lending activity will expand beyond the BRICS parameter, but for various reasons (internal and external), this process will likely happen only slowly, and patchy, mostly in Africa and Latin America. Meanwhile, the AIIB is likely to enjoy its rapid expansion, but only as a contemporary version of traditional regional bank.

Introduction

Many developing countries have long voiced their concerns about the inadequacy of development finance, particularly through the extant traditional multilateral and regional financial institutions, to address the urgent need of infrastructure development in the Global South. According to a recent estimate from an often cited World Bank study, the infrastructure investment need in the Global South is massive, some US$1 trillion a year (cited in Sun, 2015: 29). In this regard, some emerging economies have taken their own initiatives – although largely for their own national interests rather than altruistic ones – extending their own financial resources bilaterally, via their national development banks and private foreign direct investment (FDI), for infrastructure development in their fellow developing countries. Indeed, the discontent of emerging economies with traditional institutions – most notably, the World Bank and regional development banks – is an important factor that led to the recent establishment of two multilateral financial institutions: the New Development Bank (NDB) and the Asian Infrastructure Investment Bank (AIID) (Strand et al., 2016). Both of these institutions also reflect the frustration of these emerging economies with the slow pace of governance change, particularly for rectifying their under-representation (voting powers), in the "status-quo-oriented", institutionalized decision-making process of these traditional institutions.

The NDB and the AIIB were established after a relatively short "gestation" period due to two major reasons. One major reason was that the principal architects of these institutions – i.e., the parties that were involved in the negotiations on their institutional and operational details as reflected in their respective *Articles of Agreement* – were a relatively small number of Southern countries. The negotiations for the NDB were undertaken *exclusively* among five emerging economies, namely the BRICS members (Brazil, Russia, India, China and South Africa), whereas those for the AIIB were much more extensively, but basically bilateral between China on the one hand, and Asian developing countries that were interested in benefiting from the new institution on the other. The other major reason for the short gestation period was that many existing multilateral organizations provided the negotiators with institutional references (legal documents and actual operations) to reflect upon, allowed them to choose whatever they have found useful in them for their needs, and thereby made a shortcut in pursuing the task of creating new institutions.

This paper compares and contrasts the NDB and the AIIB by looking into the different paths that led to their establishment, and discusses their functional outlooks and effects on international economy. Specifically, the rest of paper consists of the following parts. Part I briefly traces the respective diplomatic background and process that brought about the establishment of these institutions. Part II compares and contrasts the major institutional similarities and differences between the NDB and the AIID as envisaged in their respective *Articles of Agreement* as well as their institutional and operational developments – though still in a state of flux – since their establishment a few years ago. Part III provides a discussion on their future outlooks and their effects on international political economy from a comparative perspective. And Part IV, the conclusion, sums up the key issues of our discussions and analyses.

Part I

Introduction to the New Institutions: Diplomatic Background & Initial Operation

New Development Bank (NDB)[1]

In April 2010 when the first meeting of the national development banks from Brazil, Russia, India and China was held, the participants signed a Memorandum of Understanding of mutual cooperation. Since then the governors of these banks (with South Africa as well from 2011) have met in what is known as the BRICS Financial Forum, parallel with the BRICS Summits (He, 2016: 3). However, it was in the broader context of the BRICS diplomatic fora between 2012 and 2014 that the concrete idea of establishing a South-South development bank gradually transformed from an ideational project (if not simply a wishful thinking) to an institutionalized entity. Specifically, at the 2012 BRICS Summit, the host country, India, proposed the idea of establishing a new financial institution. Perhaps coincidentally, China also become more active in the preparatory process of creating new institutions, particularly after President Xi Jinping came to power in 2012 (He, 2016: 3). At the 2013 Summit, the host country, South Africa showcased a new multilateral bank as the centerpiece of discussions, and the BRICS leaders then agreed to the idea of creating such an institution.

In the lead-up to the 2014 Summit (Fortaleza, Brazil), the BRICS were engaged in intense negotiations – most of all, between China and India – on the basic governance structure and operation of the new institution (see Cooper, 2016: 65-81; Cooper and Farooq 2016), and subsequently on 15 July 2014, their leaders formally signed *the Agreement of the Establishment of the New Development Bank* (*the NDB Agreement*). The NDB arguably represents the "most significant institutional innovation" of intra-BRICS diplomacy (Cooper, 2016: 65).

The ratification of *the NDB Agreement* by each of the BRICS founding members' legislative bodies – which had had occurred by March 2015 – led to the formal establishment of the new institution, in the wake of the 2015 Summit (Ufa, Russia). With the Headquarters Agreement with the Chinese central government as well as the Memorandum of Understanding with the Shanghai municipal government (the host city) in February 2016, the NDB became operational. As of this writing (August 2017), the NDB has still remained as a financial institution exclusively for the five founders.

The NDB aims at financing infrastructure projects in the private and public sectors in the emerging economies and developing countries by forgoing partnerships with national and regional development banks as well as multilateral financial institutions. The NDB began its operation with the authorized capital of US$100 billion, of which US$50 billion has been subscribed *equally* by the five BRICS founders, i.e., each with the subscription of US$10 billion. The remaining US$50 billion is to be subscribed in the future. According to official sources, during the inaugural year of 2016, the NDB approved its first set of loans – four projects, one each in Brazil, India, China and South Africa – totalling US$850 million. Reportedly, the NDB President hopes to raise the Bank's lending above US$2 billion in 2017. As will be discussed later, these actual figures announced are much smaller in scale than many early enthusiasts had anticipated.

[1] For detailed discussions on the intra-BRICS diplomatic history for the establishment of the NDB, see, for example, Cooper (2016), Cooper and Farooq (2016), He (2016), Kasahara (2016) and Stuenkel (2015).

Asian Infrastructure Investment Bank (AIIB)[2]

During the official visit to Kazakhstan in September 2013, China's President Xi Jinping, announced his country's large development blueprint of reviving the inland route of "the Silk Road Economic Belt", to link China with Central Asia, the Middle East and Europe. In the following month when he attended the Asia-Pacific Economic Cooperation (APEC) meeting in Indonesia, President Xi also disclosed yet another large development blueprint, "the 21st Century Maritime Silk Road'', to link China with Southeast Asia and, later, Europe and Africa via the Indian Ocean. These projects then quickly merged and formed the "One Belt, One Road" initiative, which, some observers readily and optimistically refer to a contemporary equivalent to the Marshall Plan (a massive American initiative to rebuild Western Europe after World War II).[3] In this regard, the AIIB is expected to play the central role in linking China and the Asian economies along the inland and maritime routes of the Silk Road (see in Yun, 2016).[4]

The AIIB proposal quickly gained momentum in late 2013, and was formally announced by China in March 2014. The proposal was discussed in May 2014 on the sidelines of the annual Board of Governors meeting of the Asian Development Bank held in Astana, Kazakhstan. On 24 October 2014, after consultation meetings among 22 Asian countries signed a Memorandum of Understanding to support the idea of establishing the AIIB.[5] Despite the United States' calls upon its allies to shun the new institution, the Great Britain made an announcement to join the AIIB in mid-March 2015 – against the application deadline (to be a founding member) of the end of the month – which induced similar announcements by many non-Asian members (Etzioni, 2016).[6] By the time of the deadline, 57 countries (37 Asian and 20 non-Asian) – known as "the Prospective Founding Members" – had indicated their commitment to being part of the process to design and establish the AIIB.

On-going negotiations[7] on *the Articles of Agreement* (*the AIIB Agreement*) ended in May 2015 (Etzioni, 2016: 174), and on 29 June 2015, 50 out of these 57 Prospective Founding Members signed

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[2] For detailed discussions on the political and diplomatic background for the establishment of the AIIB, see, for example, Etzioni (2016), He (2016), Mishara (2016), Sun (2015), Yang (2016) and Yu (2017).

[3] This is a misinterpretation and overstatement. The major goals of the United States' aid policy towards Western Europe then included to rebuild war-devastated Western Europe, to neutralize historical animosity among war-time enemies in the region, to remove trade barriers for American products, and to prevent the spread of socialism beyond Eastern Europe. According to one critical observer, the "One Belt, One Road" initiative "appears to be entirely a mercantile endeavour" (Djankov, 2016: 6).

[4] The "One Belt, One Road" initiative can be seen as an upgraded (but regionally more focused) version of China's "Go Global" policy (announced in 1999) for the new millennium though increased outward FDI. The early emphasis on securing overseas natural resources as well as markets for their manufactures seems to have been reinforced, rather than replaced, by forging additional projects in the areas of national and intra-regional transportation, power and telecommunications infrastructure (Djankov, 2016: 7; Sun, 2015: 29-30). The AIIB, according to Mishra (2016:164), could be seen as a manifestation of President Xi's idea of "Asia for Asians".

[5] Initially, China and the ASEAN members established the China-ASEAN Investment Fund (CAF), a US-dollar denominated offshore quasi-sovereignty equity fund sponsored by the Import-Export Bank of China, in 2009. The AIIB could be regarded partly as an institutional upgrading of the CAF. The early participants in the bilateral consultations vis-à-vis China included, most of all, the ASEAN members, together with several South Asian countries (Bangladesh, India, Nepal, Pakistan and Sri Lanka) as well as Central Asian countries (Kazakhstan, Kuwait, Mongolia, Qatar and Uzbekistan).

[6] Strictly speaking, the very first European country that applied for the AIIB membership was Luxemburg, which was followed by the Great Britain and many others (Menegazzi, 2017: 236). The involvement of non-regional countries, particularly many Europeans, effectively transformed the idea of the AIIB from "an obscure foreign aid agency" to a serious multilateral financial adventure, and subsequently Chinese officials purportedly, according to Yang (2016: 763-764), began to "de-emphasize" its regional orientation, particularly in terms of membership.

[7] In November 2014, 22 Asian countries deliberated on the possibility of the AIIB at the first Chief Negotiators' Meeting (CNM) in Kunming, China. During the second CNM (Mumbai, India, January 2015), the idea of *the Articles of Agreement* was put forward. Subsequently, the negotiators discussed *the Articles of Agreement* at the third CNM (Almay, Kazakhstan, March 2015) and the fourth CNM (Beijing, China, April 2015). At the fifth CNM (Singapore,

the AIIB Agreement in Beijing.[8] However, *the AIIB Agreement* did not fully reflect the concerns of all members, particularly those of the non-regional members that had skipped the earlier consultations and joined in them very late. If these donors had been given fuller opportunities of participating in formulating *the Agreement*, it would have elaborated more on the specifications of the new institution's institutional arrangement and operational modalities.

The AIIB became operational in December 2015 when the sufficient number of members – holding together more than 50% of the initial subscriptions of the authorized capital – notified their ratifications. On 16 January 2016, the AIIB was officially inaugurated. According to its *Annual Report for 2016*, the AIIB approved, in its inaugural year of 2016, US$1.73 billion in financing nine projects in seven countries in Asia. Six of them are co-financing with other institutions (such as the World Bank and the Asian Development Bank), and the remaining three are standalone. As of writing (August 2017), the AIIB's membership has grown to 80 including those whose financial contributions are under consideration.

Part II

A Comparative analysis

The NDB and the AIIB, the newest multilateral development banks focusing on infrastructure financing, have been strongly influenced by China's leadership.[9] While sharing many similarities between them as "sister institutions" with overlapping mandates, these institutions also present their own unique features that differentiate them from each other, as well as from many other existing institutions. In this section, we compare and contract these institutions under following headings: i) purposes and functions, ii) membership, iii) governance structure, iv) voting power, v) capital, and vi) borrowing. (When we explicitly note provisions of *the Articles of Agreement* in the following pages, we mean *the NDB Agreement* for the NDB and *the AIIB Agreement* for the AIIB.)

A. **Purposes and functions**

The NDB and the AIIB are very similar as far as their purposes and functions are concerned. Their respective *Articles of Agreement* underline the importance of financing projects of infrastructure and sustainable development in the emerging economies and developing economies. They both aim at forging partnerships with national development banks as well as the traditional multilateral and regional development banks, through co-financing activities in the private and public sectors. Some observers may hope that the emphasis of these institutions' financing activities for infrastructure projects, will compensate, if not reverse, the recent general trend of multilateral and regional financial institutions that have diverted their financing activities from economic development projects (Weiss, 2017: 4; see also Griffith-Jones, 2014; Reisen, 2015). Arguably, these new institutions are likely to be concerned with microeconomic viability of individual projects whereas traditional bilateral and multilateral donors may continue to pay much greater attention to macroeconomic sustainability of the borrower countries accepting their "policy-based" loans.[10]

May 2015) the chief negotiators finalized their discussions on *the Articles*.

[8] As of writing (August 2017), Brazil and South Africa – presumably due to some complex political economy problems – have still remain as "Prospective Founding Members" of the AIIB.

[9] Yang (2016: 756) argues that the NDB has been more of a collaborative effort among the BRICS members where China's role is markedly different from that in the AIIB.

[10] Policy-based loans (often in the form of budgetary support) are given typically in exchange for agreement by the borrower governments that they will undertake economic and financial reforms along liberalization, privatization and austerity.

NDB: The NDB Agreement states that the main purposes and functions of the new institution are: to finance infrastructure and sustainable development projects in the BRICS members and other emerging and developing economies (Art. 2), through loans, guarantees, equity participation and other financial instruments (Art. 3-b) in collaboration with international organizations and other financial entities (Art. 2-b). It is anticipated, therefore, the NDB will focus on microeconomic project-sustainability of individual projects whereas traditional bilateral and multilateral donors pay much greater attention to macroeconomic debt-sustainability of the borrower economies. Purportedly, the NDB's financing activities will be more geographically dispersed (at least in the long run) than the AIIB's Asian-centric counterparts.

AIIB: The AIIB Agreement states that the main purposes of the institution are to "foster sustainable economic development, create wealth and improve infrastructure connectivity in Asia by investing promote investment in infrastructure and other productive sectors" (Art.1-1), and to "promote regional cooperation in infrastructure and partnership, in addressing development challenges in the region by working in close collaboration with other multilateral and bilateral development institutions" (Ibid). Its functions include, among others, to encourage private investment in projects, enterprises and activities contributing to economic development, and to supplement private investment when private capital is not available on reasonable terms and conditions (Art. 2-iii).

B. **Membership**

In principle, the new institutions under discussion are *potentially* universal institutions. The NDB's membership is open to the member countries of the United Nations (UN), whereas the AIIB's membership is open to the member countries of the World Bank or the Asian Development Bank. However, they exhibit a clear contrast in their initial membership and expansion thereafter. On the one hand, the NDB started its operation with the five BRICS founders in 2016 and its membership has since not expanded at all. As a result, its subscription has not grown beyond the initially specified level of US$50 billion, either. On the other hand, the AIIB, of which the operation could be more regionally oriented, began its operation in 2016 with a large membership of 57 signatories (including many non-regional members), and its membership has since grown rapidly to 80 members (as of August 2017). In this regard, it is interesting to see how the membership provision of the AIIB Agreement will be interpreted. The AIIB member (presumably, central governments) can apply for membership of their "non-sovereign entities" (Art. 3-3). At this point, it is not clear what "non-sovereign entities" can include (see further discussion below).

NDB: As noted above, the NDB began with the membership of the five BRICS founders, even though its membership is open to the UN member countries, either as borrowers or as non-borrowers (Art. 5-b, 5-c). Obviously, the developed countries (e.g. OECD members) can be members, but as a non-borrower (or lenders). Emerging economy members – most of all, the BRICS – are borrowers and lenders. While in principle borrowers ought to be members as a prerequisite to get access to the NDB's funding, non-members in certain situations may receive the special authorization from the NDB to get access to its funding (Art. 19-d, 19-e). While it is not totally clear, non-borrower countries without formal membership can offer their capital markets for the NDB's bond-issuing activities. In this regard, the NDB Agreement states: The NDB is empowered "to borrow funds from member countries or *elsewhere*…" (Art. 26-a). It is not totally clear as to why the membership expansion is not taking place. One argument, which will be later discussed more, is that many countries may find that the AIIB can provide a good test case to test the membership risk prior to the application to the NDB.

AIIB: The AIIB began its operation with the membership (50 out of the 57 founding signatories), where its membership is open to the members of the World Bank as well as the Asian Development Bank (Art. 3-1). The members consist of the regional (Asian) members and non-regional (non-Asian) members (Art. 3-1-a); or of the "Founding Members" and non-Founding Members (Art. 3.1-b). Interestingly, AIIB members can apply for the membership of *their* non-sovereign entities (Art.3.3) as in the case of Hong Kong. While it is not totally clear, an implication of this provision could allow – at least theoretically – quasi-sovereign entities (such as provincial governments and state-owned enterprises) as well as private firms to become the AIIB members.[11] Let us note that China rejected the application of Taiwan, a full member of the Asian Development Bank, to be a "Founding Member" of the AIIB. China then stated that Taiwan could apply to be a "regular member" after the establishment of the AIIB, only if Taiwan should ask China's Ministry of Finance to apply for its membership (Weiss, 2017: 10). Even though the AIIB is regionally oriented, several developing countries outside of Asia, such as Brazil, Egypt, South Africa, have become members.

C. **Governance Structure**

The NDB and the AIIB share the similar four-tier governance structure: a Board of Governor, a Board of Directors, a President (with senior management), and other officials and staff, in the descending order of authority. The Board of Governors, which is represented by all member countries at the Ministerial level, is responsible for most important decisions to these institutions.[12] The Board of Directors[13] – a non-resident, non-paid entity in both institutions – is responsible, as representatives of member countries' interests, for the general conduct of the overall operation of these institutions (most importantly, granting the approval to each financing) as well as those functions delegated by the Board of Governors. As far as the regional representation at the Board of Directors is concerned, the NDB (3 out of 5, or 60%) is at this point less Asia-centric than the AIIB (9 out of 12, or 75%).[14] It should be noted, however, that the Board of Directors heavily depends on the services of bank officials and staff for loan approvals as it can be easily overwhelmed by the volume and complexity of loan operations. The President – the legal representative of the institution, and also Chairman of the Board of Directors without a voting right except the casting vote – is the chief manager, who is assisted by senior management (vice-Presidents) and other officers and staff. Due to its smaller scale of membership and operation, the NDB's governance structure – which is closely related to the voting power distribution – is much institutionally simpler than the AIIB's counterpart. Let us note that Russia, India and China have their country presentation at the Board of Directors meetings in both institutions.

NDB: The NDB began its operation of with the five-member (BRICS) Boards of Governors and Directors. Upon the approval of the Board of Governors, the Board of Directors will increase its seats up to 10 to accommodate new members (Art. 12-b).[15] The President, chosen from the BRICS on a rotation basis (Art. 13-a), heads the credit and investment committee, composed also by the *four* Vice-Presidents (and possibly more in the future), which is responsible for decisions on loans, guarantees, equities and technical assistances (Art. 13-b-ii). The posts of the Vice-Presidents are occupied by each of the BRICS that are represented as President (Art. 13-c), and the number may raise in the future with

[11] Let us note that China rejected the application of Taiwan, a full member of the Asian Development Bank, to be a "Founding Member" of the AIIB. China then stated that Taiwan could apply to be a "regular member" after the establishment of the AIIB, only if Taiwan should ask China's Ministry of Finance to apply for its membership (Weiss, 2017: 10).

[12] The substantive matters that the Board of Governors cannot relegate to the Board of Directors include those related to the admission of new members, the amendment of the Agreement (including any change of the size of capital stock), the election of the President, and others (see *the NDB Agreement*, Art. 11-b; *the AIIB Agreement*, Art. 22-2).

[13] Reportedly, China was not keen initially about the idea of creating a Board of Directors at the early stages of negotiations with Asian countries. This was probably due to the nature of bilateralism of the preliminary negotiations between China (the single donor) and potential recipients (Asian countries). However, the participation of the Great Britain with its insistence on creating a Board of Directors for the sake of enhancing the transparency of the AIIB's decision-making obliged China to change its mind (He 2016: 13).

[14] The nature of Asian centrality of the AIIB's Board of Directors is also stronger than the Asian Development Bank's (ADB) counterpart (7 out of 10, or 70%).

[15] The five founders (BRICS) will keep their "own" seat in the Board of Directors, and possibly also represent relative small new members as well in the future. For the seats beyond the initial five, new members are likely to be grouped together with others, and represented by one single country as their common representative. But the NDB allows multi-country seats to split their votes to the preferences of each constituency member (Art 6-d).

new members. The concrete details of personnel matters of the NDB that have been agreed on for the initial years are as follows: the initial chair of the Board of Governors is Russian; the initial chair of the Board of Directors is Brazilian (for four years); the first President of the Bank is K.V. Kamath, an experienced Indian commercial banker (exceptionally for six years for the first President, or for five years for the second President and thereafter) (Art. 13-d).

AIIB: The AIIB's Board of Governors began its operation with 50 of the 57 founding signatories. The Board of Directors is composed has 12 seats, responsible for the direction of the general operation of the AIIB, and performs functions delegated by the Board of Governors (Art. 26). Out of the 12 members, nine Directors are elected by the Governors representing regional members (Art. 25-1-i) and three by the Governors representing non-regional members (Art. 25-1-ii).[16] The President – presently, Jin Liqun of China,[17] – chosen from a regional member (Art. 29-1) for five years (Art. 29-2), is the legal representative of the AIIB (Art. 29-4). According to the *Annual Report for 2016*, the BIIS has established the Senior Management Team to assist the President. The team consists of five Vice Presidents (initially three from regional members and two from non-regional members) together with the General Council and the Chief Risk officer. The vice-Presidents are responsible for i) Policy and Strategy, ii) Investment Operations, iii) Finance, iv) Administration, and v) the Corporate Secretariat, respectively. As discussed later, three powerful regional members among BRICS – China, India and Russia – collectively account for overbearing amounts of financial contribution to and voting powers of the AIIB.

D. **Voting Power**

The NDB and the AIIB markedly differ from each other in the distribution of voting power in the Boards of Governors and Directors. As noted earlier, the distribution of voting powers is much simpler and much more egalitarian – as far as the BRICS founders are concerned – in the NDB than in the AIIB. However, the BRICS' total monopoly of voting power in the NDB will be reduced later with the new members' participation. Yet, *the NDB Agreement* contains safeguard provisions so that that the BRICS will retain their "dominant" position in the decision-making process in the institution. The AIIB's case is far more complicated, where the member's voting power (which reflects the relative size of its subscription) is determined mostly on its financial capacity; however, *the AIIB Agreement* also contains safeguard provisions that furnish safeguards which allow the regional (i.e., Asian) members collectively – and China singularly (see below) – to retain their "dominant" position against non-regional members.[18]

NDB: The five founding members are entitled with the same voting power (20% each) concomitant with their subscribed capital (see the discussion on the NDB's capital below), and no single member has veto power.[19] *The NDB Agreement* is not clear as to how to allocate the future contribution among the BRICS founders and new members.[20] Certainly, the membership expansion will dilute their voting power as a group. In this regard, *the NDB Agreement* contains some safeguard provisions for the BRICS: i) the voting power of the BRICS as a group will remain above 55% of the total voting power

[16] The nine Directors representing regional members are from Australia, China, India, Indonesia, South Korea, Russia, Saudi Arabia, Thailand and Turkey; and three representing non-regional members are Egypt, Germany and the Great Britain (as of August 2017, see the AIIB homepage).

[17] Jin, former Vice-President of the Asian Development Bank, served as the Secretary-General of the Multilateral Interim Secretariat (MIS), the entity responsible for preparing the legal, policy and administrative frameworks for the establishment of the AIIB.

[18] Other regional development banks, such as the Asian Development Bank, the African Development Bank and the Inter-American Development Bank, also have similar "regionally biased" arrangements (see Weiss 2017: 11).

[19] Institutional decisions require a simple majority (> 50%) of the cast votes, and those of substantive nature require an affirmative vote of two-thirds (> 67%) of the total voting power of the member countries including that of four of the BRICS members (*the NDB Agreement* Art. 6-b).

[20] The task of defining the criteria of contribution is delegated to the Board of Governors, upon which, as discussed earlier, the BRICS members will continue to have a significant control (Latino 2017: 63).

regardless of additions of new members (Art.8-c-i); ii) the voting power of the non-borrowing members, presumably developed countries, as a group cannot exceed 20% of the total voting power (Art. 8-c-ii); and iii) the voting power of any single non-BRICS member cannot exceed 7% of the total voting power (Art. 8-c-iii). Thus the BRICS are firmly guarding their pivotal position by making future "non-borrowers" individually and collectively remain minor importance with a limited voting power. While it does not seem imminent, the following situation is a possibility; If new membership is judged to threaten the 55% majority threshold of the BRICS, then the NDB will have to consider either new members' applications (including the size of their shares), or the increase of the founders' shares.

AIIB: *The AIIB Agreement* stipulates that the total voting power of each member consists of the sum of: i) basic vote, ii) share vote, and iii) in the case of a Founding Member, Founding Member vote (Art. 28-1). The basic votes, equally distributed to all members, is 12% of the grand total of all votes, i.e., the aggregation of the basic votes, share votes and Founding Member votes of all the members. The basic vote is intended to enhance the voting power of poorer member countries with small contributions (thus small share votes). The number of the share vote for a member is equal to the number of its shares of (i.e., its contributions to) the institution's capital stock. In addition, each Founding Member is allocated additional 600 Founding Member votes. As noted earlier China, the largest capital contributor, holds veto power (>25%) – a case of Super Majority – on substantive matters at the Board of Governors (Art. 28-2-i).[21] In voting at the Board of Directors, each Director can cast the number of votes to which the Governors who elected him/her are entitled and those to which any Governors who have assigned their vote to him/her (Art. 28-3). A Director can cast the vote of more than one member country may cast the vote for those members separately (Art. 28-3-i). Except some cases, all matters before the Board of Directors are decided by a majority of the votes cast (Art. 28-3.ii).

E. **Capital (authorized subscription)**

The NDB and the AIIB have started each with a total *authorized* capital of US$100 billion. Between them, however, the extent to which the members' subscriptions occupy in the authorized capital is considerably different. As for the NDB, the BRICS founders have subscribed US$50 billion of its total authorized capital, and the remaining US$50 billion has still remained unsubscribed. The AIIB's 57 Founding Members have agreed that the AIIB authorized capital are almost fully (98%) allocated among them. In other words, the NDB's subscribed capital is about half of the AIIB's counterpart. In both institutions, each member's subscription is composed of paid-in capital (20%) and callable capital (80%). Paid-in capital – which entails the actual payment over a certain period, say, over several years – is to be used to cover the sink costs for organizational build-up and associated administrative costs of the new institution, rather than directly allocated to finance development projects. Callable capital does not require the actual payment; instead, it is a sort of financial commitment, or the government guarantee that is subject to call only when the new institutions must meet obligations incurred on borrowing funds for lending. In any case, the AIIB is likely to enjoy much larger financial stocks than the NDB in the foreseeable future.

NDB: The NDB starts with an authorized capital of US$100 billion, of which the total *subscribed* capital already allocated among the BRICS founders is US$50 billion (Art. 7-a, 7-c). The "headspace" of additional US$50 billion beyond the initially subscribed capital will allow the BRICS as well as future members – without obliging the Board of Governors to amend the NDB Agreement – to subscribe to additional capital shares (Art. 7-b). The total subscribed capital for the BRICS founders is

[21] China has with the basic votes of 2,430, the share votes of 194,804, and the Founding Member votes of 600, totalling about 3000,834, or 26.1% of the total, followed by India (7.5%), Russia (5.9%), Germany (4.1%) and South Korea (3.5%). Purportedly, China was ready to reduce its voting power below the threshold of veto power (25%) if the United States and Japan had been willing to join the AIIB as Founding Members; however, neither of them turned out not to join, and China subsequently decided to secure the veto (Chin 2017: 13).

divided *equally* among them, i.e., each with US$ 10 billion. The initial subscribed capital of each of the BRICS founders is further divided into US$2 billion in "paid-in capital" (20%) and US$8 billion (80%) in "callable capital" (Art. 7-c).[22] This means that the BRICS total of "paid-in capital" is US$10 billion (US$2 billion x 5), and that of "callable capital" is US$40 billion (US$8 billion x 5). While each BRICS member is expected to make the paid-in capital over time, say, around 7 years (Art. 9-a),[23] it is not required to make such a payment for callable capital unless it is called upon to do so. As mentioned earlier, the NDB's authorized total capital at the initial stage has the headspace of US$50 billion beyond the subscribed capital of US$50 billion, which means that the new institution, in principle, can continue to raise the capital base without amending its *Agreement*. Clearly, the NDB will hold a relatively meagre amount of cash on hand for initial organizational build-up and administrative costs. It will certainly have to wait some time before reaching the position to generate any operational profits[24] and recycle them. Of course, it is easily anticipated that China (as well as its Shanghai municipality), as the wealthy host country (city) of the new institution, will provide sizable financial contributions separately to supplement the NDB's available funds to cover organizational build-up and administrative costs.

AIIB: As in the case of the NDB, the original authorized capital is divided into two parts: 20% in paid-in capital (US$20 billion)[25] and 80% in callable capital (US$80 billion) (Art. 4-2; Art.5-1). However, unlike the NDB, the AIIB's authorized capital stock of US$100 billion (Art.4.1) is *almost fully* (more than 98%) subscribed, but *unequally* allocated among the Founding Members (indicated in "Schedule A" attached to *the AIIB Agreement*). Initially 75% (or US$75 billion) of the total authorized capital was subscribed by the 37 regional founding members, and the remaining 25% by the 20 non-regional founding members.[26] China is by far the largest capital subscriber, of US$29,780.4 million, nearly 30% of the total authorized capital, occupying 26% of the total voting power.[27] The contribution

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[22] The Board of Governors of the NDB can decide not only to increase the authorized capital stock but also to alter the proportion between paid-in capital and callable capital; however, no member countries are obliged to subscribe to any part of such increased capital (Art. 7-c). The Board of Governors is also responsible for reviewing the institution's authorized capital at a 5-year interval or less (Art. 7-e).

[23] The *seven* payment instalments that each of the BRICS is expected to make are: US$ 150 million, US$250 million, US$300 million, US$300 million, US$300 million, US$350 million and US$350 million, where the first payment was expected within six months after the entry into force of *the NDB Agreement*, and the second would become due 18 months from the entry into force. Each of the remaining five will become due successively one year from the date on which the preceding one becomes due (Art. 9-a). Thus the completion of the payments of the pay-in capital may require a period up to 7 years. According to the NDB homepage, each of the BRICS members made the first instalment or tranche of US$150 million for paid-in capital subscription, totalling US$750 million in January 2016. And some of them have already made the second payment, as of writing (August 2017).

[24] How long will it take the NDB to generate the initial operational profits? Given that infrastructure projects typically carry a lending contract of 5 to 10 years, the NDB cannot expect sizeable profits from infrastructure lending for another 5 to 10 years. Thus, the earlier operational profits will be mostly from its portfolio investment using its available paid-in capital. This will not be a large amount either, because of two reasons: first, the paid-in capital will be used most of all for organizational build-up and administrative costs; and second, as discussed earlier, the paid-in capital will take another several years to complete.

[25] Each founding member is expected to make the payment of its allocated paid-in capital subscription in *five* separate payments of an *equal* amount over time (Art. 6-1). The first payment (or about US$ 4 billion in total) should be made within 30 days after the entry of *the AIIB Agreement* or on or before the date of deposit on ratification (Art. 6.1). The second payment becomes due one year from the entry into force of the Agreement, and the remaining three payments become due successively one year from the due on which the preceding payment becomes due.

[26] According to the Schedule, the headspace (unallocated portion) of the subscription for the regional and non-regional members was US$1.615 billion out of US$75 billion for the former group, US$0.2336 billion out of US$25 billion for the latter, or less than US$2 billion out of US$100 billion in total. Thus, it will be a matter of time for its Board of Governors to make a decision to raise the authorized subscription.

[27] Whereas China initially (March 2015) indicated that the AIIB would have a capital basis of US$50 billion, provided mainly by China, it changed its idea in the light of the rising interest toward it, and indicated that the new institution could target US$100 billion, including US$50 billion from Governments, and at least US$50 billion from financial institutions and private capital (see Ren, 2016). As for the distribution of the vote powers at the outset, the basic votes (12%) of the total votes are allocated equally (each with 2,430) among the member countries, the share votes

of each member is based on the size of each member's economy, with China being the largest contributors of US$ 29.8 billion and retaining the largest voting power of 300,834 (26% of the total), [28] followed by India (7.5%), Russia (5.9%), Germany (4.1%) and South Korea (3.5%). New members can join the AIIB by accepting their authorized capital subscription determined by the Board of Governor (Art. 3-2). However, the *AIIB Agreement* stipulates that unless the Board of Governors should decide otherwise, any subscription that would reduce the percentage of capital stock of regional members below 75 % of the total subscribed capital stock should not be authorized (Art.5-2). According to its *Annual Report for 2016*, the AIIB member countries as a whole had made the payment of US$6,775,305,000 for the total paid-in capital of US$18,064,400, or more than 30% by the end of the year, much faster than the stipulation of the AIIB Agreement.[29]

F. **Borrowing**

The vast majority of multilateral financial institutions have raised their long-term loanable funds by borrowing from international capital markets, by issuing bonds, against the collateral of their subscribed capital stock (paid-in capital and callable capital) as well as retained profit earnings/reserves from past operational profits (Humphrey, 2014; Kapur and Raychaudhuri, 2014; Nelson, 2013). In this regard, the NDB and the AIIB do not appear much different from these institutions that have existed. However, we may expect that the NDB's borrowing will be more geographically concentrated than the AIIB's counterpart due to the size and diversity of membership with the large number of non-regional members.

NDB: *The NDB Agreement* sets at 100% as the statutory limit on its gearing ratio: "The total amount outstanding in respect to the ordinary operations of the Bank shall not at any time exceed the total amount of its unimpaired subscribed capital, reserves and surplus included in its ordinary capital resources" (Art. 20-a). Thus at the initial stage of its operation, the maximum lending level cannot exceed the total subscribed capital of US$50 billion. With hardly any capital reserves or surplus at the outset of its operation, the NDB, in theory, is authorized to borrow up to US$50 billion and lend out by the same amount. When the remaining "unsubscribed" portion of US$50 billion in its total authorized capital is subscribed by the BRICS founders and new members, the amount of borrowing (and thus total lending) can rise up to US$100 billion (and possibly more, if profits should be made from past loans meanwhile) without amending its Agreement. Again, it is possible to anticipate that some of the BRICS founders (particularly China) may make miscellaneous contributions, additionally and separately from their paid-in capital subscription. But the NDB's paid-in capital may or may not decline as a result of its use for organizational build-up and administrative costs as well as a result of its use for portfolio investment. Whether the NDB can borrow such large amounts at reasonably low interest rates as well as find development projects to finance, however, is another question. (See the next section for the potential loaning capacity of the NDB.) At any rate, regardless of the statutory limit, the NDB may not be driven to borrow so much of funds if not many financially viable projects are proposed.

AIIB: Unlike many other parts, the *AIIB Agreement* is extremely sketchy regarding the specification of the modality of financing. This is in a way understandable since preparatory consultations,

(85%) are allocated in accordance with the size of their "shares", i.e., financial contribution (based on their economic capacity), and the Founding Member votes (3%) are allocated exclusively to the Founding Members (each with 600). China has voting power of about 300,834 (consisting of the basic votes of 2,430, the share votes of 194,804, and the Funding Member votes of 600), or as noted in the text, 26.1% of the total voting.

[28] Purportedly, China was ready to reduce its voting power below the threshold of veto power (25%) if the United States and Japan had been willing to join the AIIB as Founding Members; however, neither of them turned out not to join, and China subsequently decided to secure the veto (Chin 2017: 13).

[29] On the other hand, some AIIB signatories, including Brazil and South Africa, have not submitted their ratification, and as a result they have not paid any part of their paid-capital at all. These countries have remained as "Prospective potential Founding Members".

including the negotiations on the *AII Agreement*, was mostly bilateral between China as the finance provider and Asian recipients. Perhaps, the latter group was much careless about the process of sourcing the AIIB's loanable funds, since this would be the task of China. The AIIB may raise funds, through borrowing or other means, in member countries or elsewhere, in accordance with the relevant legal provisions (Art.16-1). Again, unlike the NDB, the *AIIB Agreement* does *not* specify any gearing ratio, i.e., the extent to which the AIIB can borrow – using callable capital and equity (paid-in capital, together with retained earnings and reserves) as collaterals – from the international capital markets. The AIIB's advantage over the NDB with its larger membership, including many non-regional countries, particularly many traditional donors with a high credit-rating status, makes it possible for the AIIB to tap more efficiently on the international capital markets.

Part III

Future Outlook

Given the recent precarious situation on the world economy (including China and other emerging economies), it is not clear whether the NDB and the AIIB will direct to any new long-term trend of international financing. In any case, let us identify and discuss some pertinent issues – which are undoubtedly inter-related – that the NDB and the AIIB are likely to face in the foreseeable future, namely i) membership, ii) lending activities, iii) loans to the private sector, and iv) concessional loans and grants.[30]

A. Membership

It seems that the NDB and the AIIB present total contrasting outlooks as far as their membership is concerned. So far, the five founding members (BRICS) of the NDB have refrained from openly soliciting non-BRIC membership. As a result, the NDB has not grown institutionally (particularly with respect to membership) as rapidly as the AIIB. Does this mean that the NDB is unable to come up with an agreed strategy in terms of its institutional development? In any case, the NDB must make its activities demonstratively attractive to draw new members, since no countries will be attracted to a nonstarter. The limited membership have so far restrained the NDB's activities in the area of co-financing with their national development banks for their own domestic infrastructure projects (see Spratt and Baron, 2015). On the other hand, China, the initiator of establishing the AIIB, actively solicited the membership. Consequently, the AIIB, which has begun its operation with a large number of Founding Members including Asian and non-Asian countries, seems likely to grow more rapidly the NDB. It may be reasonable to expect that the traditional donors that have joined the AIIB may prefer to see the benefits of their membership before deciding to join the NDC. In other words, for these donors, the membership choice between the NDB and the AIIB could be regarded as a zero-sum game.

NDB: We anticipate that the NDB will soon actively call for new memberships, before the excessive preoccupation with intra-BRICS projects dampens potential members' enthusiasm towards it. Which groups of countries will be the priority candidates as new members? The NDB's campaign may initially target at other emerging economies and developing countries over developed countries, as the former groups will likely to consolidate its pro-South solidarity vis-à-vis traditional financial institutions. But the BRICS members may not share the same view regarding which countries should be accepted as new members.[31] Between non-BRICS emerging economies and developing countries,

[30] For good discussions on the prospects (though somewhat premature and optimistic in some aspects) of the NDB and the AIIB, see Humphrey (2015), Reisen (2015) and UNCTAD (2017).

[31] One observer points out that China and South Africa are particularly interested in opening up the client base to new members, whereas India and Brazil prefer a more concentrated focus within the BRICS members (Cooper, 2016: 76). Technically speaking, non-member countries, in exceptional cases, may still obtain funding from the NDB

the priority may lies in the former group, as they can provide the NDB with larger capital contributions, less risky investment opportunities and more reliable capital markets. So far, no traditional donor countries have openly indicated their intention of participation. The BRICS founders (and future borrower members) may feel that the participation of non-borrower countries should be welcome because it will augment its capital base and raise the possibility for the NDB to improve its access to international capital markets. Whereas the membership growth with non-borrower countries, even as minority stakeholders, is also likely to raise the new institution's credit rating, it will dilute the ideational foundation of the NDB as an institution of South-South cooperation. In any case, non-borrower countries may consider that they should not harry to join the NDB, preferring to take a wait-and-see stance. Countries that are very likely to join the NDB are those that are not major beneficiaries of the AIIB, namely the non-Asian developing economies, particularly those in Africa and Latin America. Their participation in the NDB will heavily depend on the effective representativeness of South Africa and Brazil for their respective region. One possible implication of the likelihood of new membership from Africa and Latin America is the possible rise of influence of South Africa and Brazil in the decision-making process. This is because in the Board of Directors the South African Director and the Brazilian Director are likely to represent their respective region's smaller members.

AIIB: The AIIB's initial membership of 57 Founding Members, with the notable absence of the United States and Japan, has been already a good indication for the future prospects. Given its large membership (including many traditional donor countries) and China's active leadership role, the AIIB may eclipse the NDB in the long run (Cooper, 2016: 78; also see Humphrey, 2015). On the other hand, non-regional developing countries may perceive that their membership in the AIIB would be far less significant. As a matter of fact, there are only a few non-regional developing countries – such as those from Africa and Latin America[32] – have joined the AIIB. For these countries, their AIIB's large membership (thus the intense competition among beneficiaries) would reduce the potential benefit that they enjoy. Many of developed countries have already joined the newly established AIID, and they may prefer to monitor its performance to judge whether they should join another similar institution.

B. Lending activities (quality and quantity)

It is wondered how soon the NDB and the AIIB will develop their "independent" operation, departing from being the "disguised" figureheads engaged as operational arms of national development banks or as co-financing, free-riders for existing multilateral financial institutions.[33] Some developing countries may expect that in the name of South-South cooperation, these new institutions will make "faster, simpler and cheaper" disbursement of loans. The NDB and the AIIB, particularly the former due to its small membership, may be able to come up with a novel, more flexible approach to avoid the negative associations with "old" conditionality. If they should successfully achieve this, then their popularity will surely rise among would-be borrower countries, and their operation as well as membership will expand.[34] Let us note that both the NDB and the AIIB have signed Memorandums of Understanding

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without prior membership. Nevertheless, given that formal membership eases the project evaluation and financing process, the BRICS members are likely – again with different degrees of eagerness – to solicit new membership. In any case, the formal membership of these countries will also help them participate in the NDB's governance process as well as increase its capital base (Griffith-Jones, 2014: 13).

[32] The recent establishment of the NDB's Regional Office in Johannesburg, South Africa (August 2017) is likely to raise its lending activities in South Africa as well as Africa as a whole, which in turn invite a greater participation in the NDB from the continent. Similarly, Brazil has had informal discussions with the NDB administration on the idea of establishing Latin American's regional office in Sao Paolo (see various Press Releases from the NDB homepage).

[33] The new institutions, particularly the NDB, with the virtue of being relatively small entities at least at the outset, are likely to impose far less bureaucratic red-tape and possibly shorter loan approval processes than many existing institutions.

[34] However, membership expansion also implies greater bureaucratization of the institution, which tends to slow down the approval process. (For an excellent comparative analysis on three multilateral development banks, see Humphrey and Michaeloa, 2013). At any rate, no multilateral development banks have ever called in callable capital to cover their losses (Nelson, 2013: 9). Rating agencies, in fact, regard callable capital – more specifically, that of

with many national and international financial institutions.[35] As discussed below, some preliminary exercises, such as Griffith-Jones (2014), Reisen (2015) and Humphrey (2015), of estimating the potential lending of the NDB and AIIB based on different methodologies and assumptions, present optimistic prospects. As a result, Reisen, for example, optimistically – or unrealistically – concludes that these institutions could have "a discernible impact on multilateral lend, and thus on global governance" (Reisen, 2015: 302). While it is admittedly difficult to come up with accurate estimates of these institutes' lending, our estimates are more modest than these referred estimates. Yet, as the AIIB seems to enjoy greater institutional development than the NDB, the former institution is also likely to lending more than the latter.

NDB: The NDB's present concentration on the BRICS's own projects may seriously constrain lending to poorer countries, which will add to the possibility of tension and discontents among would-be borrowers.[36] This is the dilemma that the NDB may be confronted with. The NDB's loans are purportedly free of a strong dosage of political conditions, certainly those related to institutional reforms for augmenting good governance, promoting human rights, and preventing corruption in developing countries. But as the NDB increasingly co-finances with other institutions (beyond the BRICS's national development banks) and raises its loanable funds widely (and cheaply) from international capital markets beyond the BRICS members, it will follow conventional international banking standards, "sound banking standards principles". Even if these new institutions should be willing to take those "higher" risks, its loan contracts would be likely to contain "prudential conditionality" provisions to ensure that loans are used purposely and rapidly. This means that the NDB (as well as the AIIB) will be obliged to impose similar efforts – of project-specific microeconomic conditionality – on the part of borrower countries, just as existing multilateral and regional development banks have practiced.

Griffith-Jones (2014) was one of the first scholars that bravely ventured into estimating scenarios of loaning activities of the NDB. Based on a few assumptions,[37] she came up with the estimations that the NDB will lend (with average maturity of ten years) of about US$5 billion per year during the first 10 years, and US$7 billion annually thereafter. These figures show an extremely large size of lending by a new institution. Reisen (2015) estimates that how large the loan portfolios (outstanding and undisbursed) of the NDB will be when their respective members' pay-in capital is completed. He points out that as of March 2015, the World Bank has the total loan portfolio of US$152 billion against the total paid-in capital of US$14 billion with the loan/paid-in capital ratio of 10.9. Arguing that the NDB would cover a potential borrower groups similar to the World Bank. Reisen states that the NDB would potentially have the loan portfolio of US$109 billion (US$10 billion x 10.9) when the paid-in capital is completed (in several years).[38] Amazingly, this implies that the NDB's loan stock will *potentially* reach about two-thirds of the World Bank's present stock. Humphrey (2015) presents various scenarios of the NDB's loaning activities based on more detailed and additional assumptions. All of his estimates, including the most optimistic ones, turn out to be somewhat smaller in scale than

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industrialized non-borrower member countries – of multilateral development banks as "unequivocally the main criteria" (Humphrey, 2014: 618-9) to determine their credit rating.

[35] These memorandums highlight potential common areas of interest, not only exploring and pursing opportunities for co-financing projects but also facilitating knowledge exchange, staff secondment and exchange.

[36] But the NDB will likely prioritise high quality loans for its founding members in order to minimize the risk of default. Indeed, the BRICS members must be aware of the potential implications of the NDB's performance on its credit rating, which, in turn, will affect the costs of its borrowing and the generation of profit levels necessary to support future lending (Griffith-Jones, 2014: 8).

[37] They include the NDB's subscribed capital being already at US$100 billion (instead of US$50 billion) at the initial stage of operation, and the loan-equity leverage ratio (the ratio of the outstanding loans against the total paid-in capital of US$20 billion with retained profit earnings and other reserves) being 240%. Therefore, these figures will prove to be overestimations, unless new members (with large financial capacities) should quickly join the institutes

[38] Reisen could have assumed that the NDB's paid-in capital would be US$20 billion rather than US$10 billion. At least, this would be the 20% portion of its total authorized capital. Thus, the total loan stock of the NDB could have been estimated to be US$218 billion (US$20 billion x 109).

those presented by Griffith-Jones (2014) and Reisen (2015). His estimates for the NDB's *cumulative* loan portfolio are in the range of US$45-65 billion over the first seven years as opposed to Griffith-Jones' estimates of US$5 billion per year during the first ten years and US$7 billion per year during the second ten years, or Reisen's estimate of US$109 billion in seven years after launching operations. Humphrey thinks that the amounts of the NDB will be "relevant but fairly modest" in relations to existing multilateral development banks, and will not be a global "game-changer" (Humphrey, 2015: 30).

In our estimates, the NDB will probably make loans of a few billion dollars at most a year for several years. When countries (particularly non-borrower countries) apply for their membership, the NDB will determine the size of their individual capital subscriptions, and review its total authorized capital (of initial US$100 billion). It is only at that occasion, if that ever happens at all, that the NDB will face a real opportunity of raising its lending capacity substantially. As mentioned in Part I of this paper, in 2016 the NDB approved its first set of loans – four projects, one each in Brazil, India, China and South Africa – totalling US$850 million. Reportedly the NDB President hopes to raise the institute's lending above US$2 billion in 2017. Needless to say, these figures announced by the NDB are much smaller in scale than these estimates mentioned above.

AIIB: We have already witnessed the initial wave in the AIIB's investment activities which are collectively much larger than the NDB's counterpart. So far, most of the AIIB's projects are those located in countries related to the "One-belt, One-road" initiative. An estimate of the loan portfolio of the AIIB by Reisen (2015) indicates that the institute would have the portfolio (outstanding and undisbursed) of US$ 127 billion when the paid-in capital is completed (in several years).[39] This was based on the assumption that the institute would follow the lending practice of the Asian Development Bank. This means that the AIIB's loan stock will reach more than one and a half times the Asian Development Bank's present stock. He optimistically – or unrealistically – concludes that these institutions could have "a discernible impact on multilateral lend, and thus on global governance" (Reisen, 2015: 302). Based on different assumptions, Humphrey (2015) presents several scenarios of the AIIB's outstanding loan portfolio over the 2016-2025 period, which states that the outstanding loan portfolio in 2015 will amount to be where between the lowest sum of US$65.3 billion to the highest of US$127.6 billion.

C. Loans to the Private Sector

Both the NDB and the AIIB do not consciously distinguish infrastructure projects undertaken by the public sector and by the private sector. This is also the case of the Inter-American Development Bank.[40] For private sector investment these new institutions are likely to co-finance with existing international financial institutions and others that have some track record in this area. This operation would resemble the dominantly private-sector oriented financing of the European Bank for Reconstruction and Development (EBRD) established in 1991 to facilitate the market-oriented transition in East European economies as well as the former Soviet Republics. However, the relative weight of private sector projects in these new institutions' financing does not seem to be as significant as that in the EBRD.

NDB: The NDB's functions include, among others, "to support infrastructure and sustainable development projects, public and private, … through the provision of loans, guarantees, equity

[39] Reisen clearly errored assuming that the AIIB's paid-in capital would be US$10 billion, instead of US$20 billion. Thus the total loan stock of the AIIB could have been estimated to be US$254 billion (US$20 billion x 127). It should be also noted that Reisen's assumption of the likelihood that the AIIB will follow the lending practice of the Asian Development Bank could be questioned, as the new institution includes many developing country counties in central Asia that do not belong to the latter bank.

[40] For a useful overview of lending activities and institutional arrangements of major multilateral development banks, see Nelson (2015).

participation and other financial instruments" (Art 3-a); and "to cooperate … with international organizations as well as national entities whether public or private, in particular with international financial institutions and national development banks" (Art 3-b). Regarding its methods of operation, the NDB "may guarantee, participate in, make loans or support through any other financial instruments, public or private projects, including public-private partnerships, in any borrowing member country, as well as investment in equity, underwrite the equity issues of securities, or facilitate access to international capital markets of any business, industrial, agricultural or service enterprises with projects in the territories of borrowing member countries" (Art 19-a). Thus, the NDB is expected to get involved in public and private projects; however, its Agreement does not specify the different conditions of financial disbursement between public and private sector projects.

AIIB: *The AIIB Agreement* stipulates that the new institution may "provide or facilitate financing to any member, or any agency, instrumentality or political subdivision thereof, or any entity or enterprise operating in the territory of a member …" (Art. 11-1-(a)). And its operation can include, among others, investing "in equity capital of an institution or enterprises" (Art. 11-2-(ii)). Let us recall that *the AIIB Agreement* could accommodate the membership of "non-sovereign entities", which means that – depending on the interpretation of the term – state-owned enterprises and private firms may be included as full-fledged members.[41] If that should turn out to be the case, then the private sector financing will be further encouraged.

D. Concessional loans and grants

While multilateral institutions, as main line of operation, provide loans carrying interest rate and repayment requirement similar to commercial lending, soft loans (or concessional loans) with below market-based terms as well as grants with no repayment obligation have also occupied important components of their operation particularly to low-income countries. For instance, the World Bank started its operation in 1946 to provide "non-concessional" lending to middle-income countries and creditworthy low-income governments, but pressure from developing countries made the major western powers agree to create a soft-loan window, the International Development Association (IDA)[42] – which has so far not raised any funds in the international capital markets (Reisen and Zattler, 2016: 3) – to provide concessional loans and grants to low-income countries. In fact, major regional development banks have established their soft loan window, whose is rather small relative to non-concessional counterpart, and its resources come mostly from periodic replenishments by donor countries (rather than bond issuances). It is perhaps a matter of time that the AIIB will establish an autonomous (or semi-autonomous) concessional window just as many other regional development banks.[43]

NDB: While details are not elaborated on, *the NDB Agreement* postulates that the new institution's overall loaning activities consist of "ordinary operation" – presumably non-concessional loan – which is financed from the ordinary capital resources, and "special operation" – presumably concessional loan – which is to be financed from the Special Funds resources (Art. 18-a). It is anticipated that once poorer countries, particularly those in Africa begin to join the NDB, they will ask for concessional loans. Given that the BRICS members, particularly China, have increasingly been involved in

[41] However, this would create a new problem of capital prescription associated with membership. It is unknown if non-sovereign entities could participate in the AIIB without subscription.

[42] Let us note that China decided in 2007 to become a new donor to this institution (Xu and Carey, 2015: 1).

[43] The African Development Bank, which was established in 1964, created its concessional lending window, the African Development Fund, in 1972. Whereas concessional lending grew rather slowly for a while, its official opening to non-regional contributing members in 1982 brought about a rapid growth of such lending. The Asian Development Bank, which was established in 1966, also created its concessional lending window, the Asian Development Fund, in 1973. Since its establishment in 1973, the Inter-American Development Bank has had both the non-concessional and concessional windows, with the soft loan window being called the Fund for Special Operations. The European Bank for Reconstruction and Development does *not* have a concessional loan window, as hardly any countries in the region is classified as a low-income country by the World Bank.

concessional lending in their own bilateral South-South cooperation activities, they may not find much merit in bringing the issue of concessional lending with presumably more time-consuming negotiations to the NDB's operation. The BRICS members may prefer to use their new institution for non-concessional lending, and let concessional lending be handled on a bilateral basis.[44] As stated above, we expect that the NDB's concessional lending window will not issue bonds and that it will instead use funds contributed directly from their member countries (replenishments), as well as retained earnings, for the operation of non-concessional lending. Needless to say, the latter option is not possible at the early stages of operation when the NDB has not generated profits. Thus, poorer countries may choose to defer their participation in the NDB until the institution becomes able to finance such preferential financing. After all, if these countries can expect concessional loans bilaterally from some BRICS members, they may continue to rely on bilateral channels of concessional loans rather than switch to multilateral channels. On the other hand, low-income countries may view that the NDB can provide an institutional merit of diluting bilateral donors' political influence over recipients' decision-making.

AIIB: As in the case of the NDB, *the AIIB Agreement* contains the provision on Special Funds, presumably concessional loans, which are "designed to serve the purpose and come within the functions of the Bank" (Art. 17-1). However, it lacks clarity. The Agreement states that the AIIB "shall adopt such rules and regulations as may be required for the establishment, administration and use of each Special Fund" (Art. 17-3). As noted earlier, if the AIIB should follow the lending modalities of the major regional development banks, then it would be a matter of time for the AIIB to establish an autonomous (or semi-autonomous) concessional window to handle "special funds" just as some regional development banks – such as the African Development Bank, the Asian Development Bank and the Inter-American Development Bank – have done earlier. However, the institutionalization of a soft-loan window would likely entail a new phase of consultations among the AIIB members at the level of the Boards of Governors and Directors. The main issue of contention – particularly between non-regional (donor) members and the main contributor, China – would be the task allocation of additional contributions (replenishments) to the special funds. Arguably, China may prefer to keep its concessional loan operations in its own bilateral channel, rather than bring them under multilateral scrutiny of the new institution.

Part IV

Conclusion

Given that aid commitments from traditional donors and their development institutions have not been able to effectively address the infrastructure bottlenecks in the Global South, any additional funds, including those from the NDB and the AIIB, should be welcome. These institutions should be encouraged to promote the process of overcoming these bottlenecks so that the fund recipients can tap their development potentials more effectively. After all, the stock of productive assets – particularly a wide range of transport and energy-related infrastructure assets – are likely to bring about positive impacts, as they, among others, reduce the costs of production and marketing (domestically and internationally). These new institutions, however, have not been free from serious debate. One major point of contention is the question of additionality (or supplement arity), i.e., to what extent the financing by the NDB and AIIB can constitute a net addition to the international financial flows for infrastructure development in the Global South. The answer to the question of additionality may have a lot to do with the perception regarding whether the financing activities of these new institutions should be seen as alternative or supplementary resources to those of the traditional institutions.

[44] On the other hand, even if some of the BRICS members (particularly China) can secure resource supplies and market outlets for their economies through bilateral lending, they may encourage borrower countries to join the NDB. This is because, the funding through multilateral institutions, such as the NDB, enables risks to be pooled, limits reputation costs, and increases the perceived legitimacy (Dixon, 2015: 4).

The NDB founders – the BRICS members – have often advocated horizontal, South-South solidarity as the institution's ideational foundation, which has offered a comforting rhetoric to many developing countries which may be interested in joining them. In fact, the NDB has been institutionalized so far, as a partnership organization of equals among its founding members, where each BRICS member is entitled with an equal amount of capital subscription. If this equality principal should persist, its capital stock will be heavily determined by the weakest BRICS member, South Africa. Thus, unless this smallest BRICS member cannot manage to obtain funds – say, for example, from other BRICS members – to cover the payment of its subscription, the new institution will remain too small to make a serious difference. In that event, one way to make the NDB large enough to matter is to encourage major Northern donors' participation, but this will make the NDB, as in the case of the AIIB, resemble existing multilateral organizations. If the NDB should decide to raise its lending but at the same time to eschew the option of extensively admitting non-borrower countries, then it will have to compromise the principle of equality by letting China, the only one with the financial clout among the BRICS members, raise the NDB's overall capital stock. In that event, it is very likely that China – as the United States did for the World Bank in the 1940s and 1950s – will ask for more commensurate power in the institution's governance (Kapur and Raychaudhuri, 2014: 16).

The AIIB has begun its operation with a large membership, arguably the largest (with 57 members) at the time of birth compared with other regional organizations. In contrast to the NDB, its lager membership has also contributed to a larger operational and lending scale. However, the participation of many traditional donors (mostly as non-reginal members) have complicated the task of resolving internal differences and forging a coherent package of institutional strategies acceptable to all. Some early observers, particularly prior to the European announcements of participation, viewed the AIIB as a concrete manifestation of South-South cooperation, and expressed their hope that this new institution would manage their operations differently from the mainstream development institutions. Now, few observers stress the merit in the management of the AIIB of sustaining the principle of non-interference, a major element of South-South solidarity.

Some observers still expect that both the NGB and the AIIB will continue to refrain from imposing severely intrusive conditions of political and economic nature on their member countries. This is because such conditions (particularly, in the case of the NDB) – which covers governance, macro-economic policy and performance, and institutional reforms – contradict the principle of respecting national sovereignty (perhaps, most importantly country-ownership of reform). However, as these new institutions undertake large-scale commercial activities around the world, the absence of concern with the agenda of building effective states within loan-recipient countries may prove to be the defect rather than the merit of their operation. Obviously, all contemporary financial institutions – whether national, multilateral, or regional types – have to take in consideration as issues of political and regional security issues (see, for example, Cary and Li, 2016; Lipton, 2017). The future participation of traditional donor in these institutions (already in the AIIB) will make these institutions resemble the mainstream multilateral institutions.

China, India and Brazil have been among the top borrowers from the World Bank. China and India are also similarly among the top borrowers of the Asian Development Bank. Then it is wondered to what extent the NDB and the AIIB will reduce these emerging economies' reliance on these traditional institutions. We do not expect a major reduction, particularly in absolute terms in the near future. We foresee that these new institutions will, in the foreseeable future, continue to supplement (particularly through co-financing) rather than replace existing institutions. Senior staff of these new institutions are expected to be engaged regularly in exchanges of views on best practices with their counterparts of major multilateral financial institutions. Such exchanges will be important not only to avoid various risks, such as inefficiencies, occupational overlap, and perhaps most importantly the turf war, but also to cause a greater convergence of operation mode, These new institutions, particularly the AIIB, may consequently end up with the same role which they have often accused the existing institutions of playing.

In sum, we recognize that official assistance from traditional donors (bilaterally or multilaterally) have failed to meet financial needs of many developing countries to overcome their infrastructure bottlenecks. In this regard, the expansion of lending activities of the NDB and the AIIB will enable the increasing number of developing countries to cope with their infrastructure deficits and tap their development potentials. We certainly expect that the operational scale of the new institutions will be widened, but at the same time we foresee that this will be a slow and unsteady process. The most optimistic forecasts indicate that these institutions' lending will amount to a fraction of the overall need of infrastructure development in the developing countries. It is unrealistic to expect that poor countries with few natural resources will suddenly be able to get access to sizeable, additional lending from them. If developing countries should perceive that the new institutions (particularly the NDB) fail to create recognizable impacts on the infrastructure bottlenecks and/or bring forth significant changes in the international financial architecture, they would question the merit of reinventing the wheel. Even worse, they may even regard these new institutions as an institutionalized smokescreen to the advantage of the emerging economies – particularly China[45] with overwhelming foreign reserves and active construction firms – to hide their acts of exploitation in fellow developing countries.

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[45] After all, China has felt the need to diversify its massive foreign reserves away from its investment in the Treasury Bills of the United States (Cooper and Farooq, 2016: 85).

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