

# Rational Institutional Design of the Asian Infrastructure Investment Bank:

## Bounded Rationality Embedded in A Change-through-Continuity Characteristic

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## **ABSTRACT**

As a Chinese initiative, the Asian Infrastructure Investment Bank (AIIB) is a newly established multilateral financial institution which addresses the daunting infrastructure demands across Asia and furthers interconnectivity and economic development through advancement in infrastructure and other productive sectors. AIIB is envisaged to be built into a first-class multilateral development institution with 21st century governance, to cooperate with and be complementary to existing financial institutions. Therefore, this thesis aspires to capture an in-depth understanding of the AIIB by answering the questions ‘what is the characteristic of the institutional design of AIIB, in comparison with Bretton Woods institutions and Asian Development Bank (ADB), and what corresponding role China has played in contributing to its institutional design feature?’ This thesis relies primarily on the official founding documents of the institutions, applies thematic analysis as data analysis method, and further employs key concepts from rational design on international institutions including membership, scope, centralization and voting, to interpret and analyze data. This thesis finds out that change-through-continuity is a recurring characteristic of the AIIB’s institutional design, in which China being a revisionist reformist has played a significant role in shaping its characteristic. These findings contribute to the conclusion that the change-through-continuity characteristic of AIIB’s institutional design is a manifestation of bounded rationality.

**Key words:** AIIB, Rational Institutional Design, Bounded Rationality, China, IMF, World Bank, ADB

## PREFACE

彼采萧兮...美目盼兮...

Strolling by the riverside of Dora in Turin, I never expected that a casual talk on the Asian Infrastructure Investment Bank with my summer school colleagues would lead me all the way to extensively engage with it for nearly a year. For me, the AIIB is something old, something new, something down-to-earth, and something rather ambitious.

My personal story with AIIB is coming to an end. In retrospect, the most heartfelt thanks shall go to Stefan Brehm, my supervisor, for your valuable insights and constructive feedback on my thesis. I am truly grateful for your inspirational support.

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I owe my deepest gratitude to my family back home. I especially dedicate this thesis to my beloved parents for being incredibly supportive and understanding all the way along; The last two years have been a rewarding and precious journey for me to be surrounded by your unconditional love and support; As for myself, it is an unforgettable process of initiating in-depth conversation between what I used to be and what I am going to be, and I feel grateful for having this tranquil period of self-reflection and self-growth.

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Enjoy!!

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## ACRONYMS AND ABBREVIATIONS

ADB	Asian Development
AIIB	Asian Infrastructure Investment Bank
AOA	Article of Agreement
APEC	Asia-Pacific Economic Cooperation
BRICS	Brazil, Russia, India, China, South Africa
CCIEE	China Center for International Economic Exchange
CNY	Chinese Yuan, or Renminbi
CPC	Communist Party of China
ESF	Environmental and Social Framework
EU	European Union
GDP	Gross Domestic Product
IBRD	International Bank for Reconstruction and Development
IMF	International Monetary Fund
KLP	Keeping A Low Profile
MDB	Multilateral Development Bank
MFA	Ministry of Foreign Affairs
MOU	Memorandum of Understanding
NPC	National People's Congress
OBOR	One Belt One Road
PRC	People's Republic of China
ROC	Republic of China
SCTAO	State Council Taiwan Affairs Office
SFA	Striving for Achievement
U.S.	United States
UNECAFE	United Nations Economic Commission for Asia and the Far East

# CHAPTER 1 INTRODUCTION TO THE ASIAN INFRASTRUCTURE INVESTMENT BANK (AIIB)

## 1.1 Background and Context

Initiated and promoted by China, the Asian Infrastructure Investment Bank (hereinafter, AIIB or the Bank) is a newly established multilateral financial institution, which is specially tailored to bring countries together to address the daunting infrastructure deficits across Asia, and featured by its goal of furthering interconnectivity and sustainable economic development in the region through advancements in infrastructure and other productive sectors, and stimulating growth and improving access to basic services.<sup>1</sup> The AIIB has adopted the core principles of openness, transparency, independence and accountability, along with the modus operandi of being ‘Lean, Clean and Green’.<sup>2</sup>

A few background stages are of importance to understand the initiation, establishment and operation of the Asian Infrastructure Investment Bank (AIIB) in the four years proceeding 2013.

*Proposal:* The original idea for the creation of an “Asian Infrastructure Investment Bank” was initially proposed by Zheng Xinli, the Vice Chairman of the China Center for International Economic Exchanges(CCIEE) at the Bo’ao Forum in April 2009, to advocate for an optimal use of Chinese foreign currency reserves and addressing infrastructure issues in Asian countries against the backdrop of the global financial crisis.<sup>3</sup>

*Announcement:* The AIIB initiative was essentially announced during President Xi Jinping and Premier Li Keqiang’s visits to South-East Asia when they collectively proposed the AIIB to their hosting nations in October and November 2013.

*Consultation and Negotiation:* Bilateral and multilateral consultations and negotiations were subsequently underway in relation to the core principles and major elements for the establishment of the bank. There were eight chief negotiators’ meetings on the establishment of the Bank in total held to collaboratively engage with

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<sup>1</sup> AIIB <https://www.aiib.org/en/about-aiib/index.html> Asian Infrastructure Investment Bank(AIIB), 2017. About AIIB. [online] Available at: < <https://www.aiib.org/en/about-aiib/index.html>> [Accessed 10 January 2017].

<sup>2</sup> Lean means a small efficient management team and highly skilled staff; Clean means an ethical organization with zero tolerance for corruption; and green means an institution built on respect for the environment.

<sup>3</sup> Bo’ao Forum, 2009. *Expanding Economic Cooperation in Asia, Helping the Globe Get Rid of Crises*. [online] Available at: <<http://english.boaoforum.org/mtzxxwz xen/1966.jhtml>> [Accessed 28 March 2017].

the preparatory works, including various operational policies such as public information interim policy environmental and social framework, and strategies and business plans such as thematic priorities and strategic programming.

*Inauguration and Operation:* On January 16, 2016, the Board of Governors of the AIIB convened its inaugural meeting, and declared the Bank open for business, and meanwhile Mr. Jin Liqun was elected as the President of the Bank for a five-year term.<sup>4</sup> Since start of operation, at the time of finalizing my thesis, there are currently 13 projects approved and 12 projects proposed.

Traversing the stages of initial proposal, official announcement, bilateral and multilateral consultation, inauguration and operation, the Bank has been garnering worldwide sensation, diverse interpretations and investigations.

## 1.2 Research Question

In the light of the aforementioned context, the body of research on the Bank is rather nascent but increasingly burgeoning, varying from studying the underlying causes and conditions of China's proactive move to establish the Bank, to the Bank's challenges and prospects concerning governance and operation, to the dynamics and potential ramifications for international financial architecture, and global economic governance. Considering this, there is little academic value in simply replicating the previous research. It is therefore of importance for a more comprehensive and in-depth analysis of the Bank itself. The aim of this thesis is to investigate and explain the understudied but pivot question, namely, the Bank's institutional design against the backdrop of China's official visions for and roles within it. Two overriding **research questions** are raised:

- 1) In regards to institutional design, what is the characteristic possessed by the Bank, in comparison to the International Monetary Fund (IMF), World Bank (narrowly refers to IBRD) and Asian Development Bank (ADB)?
- 2) What corresponding role has China played in contributing to the characteristic of the Bank's institutional design against the backdrop of Chinese official visions in relation to the Bank?

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<sup>4</sup> Asian Infrastructure Investment Bank(AIIB), 2016. *Jin Liqun elected as first President*. [online] Available at: <[https://www.aiib.org/en/news-events/news/2016/20160116\\_002.html](https://www.aiib.org/en/news-events/news/2016/20160116_002.html)> [Accessed 19 January 2017].

There are a series of subordinate questions attached to be raised beforehand as well. They include: What are the exact dimensions to be examined in the institutional design to observe its design characteristic? What are China's official visions and its underlying social structures in relation to the Bank? To what extent do the characteristics of the Bank's institutional design reflect the Chinese official visions and advocacy?

### **1.3 Research Aim and Contribution**

This thesis aspires to capture a nuanced understanding of what characteristic AIIB represents in the aspect of institutional design, through a comparative analysis with IMF, World Bank and ADB and China's corresponding role in shaping its institutional design. A sound and comparative inquiry into the Bank's institutional design in the *status quo* could be conducive to analyzing efficiency and accountability of its current operation and governance, also providing the background knowledge for possible scenarios regarding its future reform and institution trajectory. In this sense, this thesis will be a valuable addition to broaden and deepen up the existing body of research in regards to the Bank's institutional design.

It is notable that the majority of existing bodies of research on the Bank lack a robust theoretical framework, despite the fact that some studies have generally adopted a theory but proceeded in an *ad hoc* and insufficient manner in the subsequent data analysis. Considering this, one of the major contributions of this thesis is estimated to offer a more systematic theoretical analysis.

Last but not least, the previous research has generally exhibited an inclination to approach the Bank in a speculative fashion, and thus the validity and sources of the argumentation is not that convincing. Compared with that, the research materials and sources are more transparent and accountable when conducting research on the Bank's institutional design, by virtue of the fact that the main research resources, including the Articles of Agreement, governance policy, operational policies and strategies, and projects information, are accessible, transparent and reliable on the official websites of the research subjects.

### **1.4 Previous Research**

The previous research shall be attentively and thematically reviewed, in order to show

how the existing literature paves the way for advancing the analysis of the Bank's institutional design in the forthcoming chapter. There are three thematic strands of literature review in close relation to this thesis: 1) underlying accounts and conditions of creating AIIB; 2) internal dimensions of AIIB; and 3) manifestation of assertive and normative China.

*The underlying accounts and conditions of creating AIIB*

Scholarly interest in China's underlying motivation for dedicatedly pushing forward AIIB, from its initial announcement to successful debut through rally of regional support, and the refinement of AIIB's role and assuagement of outside concerns and doubts, has witnessed a surge. It has been widely unscrambled from the lenses of China's domestic political economy, unstable external environment, perceived representation or voice gap in the global economic governance along with increasingly outspoken grand strategies.

From a domestic point of view, Yong Wang offers a broad investigation about the rationality of initiating the AIIB in line with the One Belt One Road strategy, by arguing that the creation of these initiatives was partially driven by the pressure of the ongoing slowing down of economic growth internally, labelled as a 'new normal' (新常态),<sup>5</sup> and the AIIB is a feasible outlet to digest the problems of overcapacity and excessive foreign reserve, by carrying forward international economic cooperation projects through infrastructure construction.<sup>6</sup> This is a sound argument to reflect the side-effects of China's pains-taking effort in coping with the 2008 global financial crisis. However, this view offered by Yong Wang is further enriched by Daniel Chow, who argues that the AIIB could be beneficial specifically to China's massive SOEs for successfully bidding for infrastructure projects under the auspices of the China's dominant role in the AIIB.<sup>7</sup> Similar to this constraint-solution approach, Chen additionally pinpoints another underlying account, namely, utilizing the Bank as a proper financial platform to internationalize Chinese currency; *Renminbi* (CNY).<sup>8</sup> However, this argument still remains contested or at least unclear, due to the bank

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<sup>5</sup> "New Normal" is a concept used by Chinese leaders and economists to describe the ongoing slowing down of growth to around 7.0 percent GDP a year as well as the forbidden tasks of transforming the growth model from one driven by exports and investment toward one driven by domestic consumption.

<sup>6</sup> Wang, Y., 2016. Offensive for defensive: the belt and road initiative and China's new grand strategy. *Pacific Review*, 29(3), p. 457.

<sup>7</sup> Chow, D., 2016. Why China Established the Asia Infrastructure Investment Bank. *Vanderbilt Journal of Transnational Law*, 49(5). p.1258-1264.

<sup>8</sup> Chen, H.J., 2016. *The Comparative Political Economy of Asian Infrastructure Investment Bank's Development: An Analysis of Neo-Institutionalism*. Master of Arts. National Cheng Kung University. p.60-62.

currently adopting the official currency of payment of the United States of America, in accordance with the AIIB Articles of Agreement.<sup>9</sup>

From the view of China's external environment, Yong Wang argues that the AIIB as one element of China's systematic OBOR strategy, is seen as a response to the 'pivot to Asia' policy employed by the U.S. and its deteriorating bilateral relations with neighboring countries, and a counterbalance for allowing for more strategic maneuvering space for China to change to a relatively passive position in coping with the accumulative U.S. pressure.<sup>10</sup>

In a similar vein, China's official perception of its unstable external environment is also manifested by its perceived representation or voice gap in the global economic governance. On this matter, Daniel Chow has conducted an interesting inquiry by arguing that China is perceived as poorly treated and deliberately contained by the United States and has found no realistic possibility of playing an expanded part in the IMF and World Bank more commensurate with its economic weight in the global economy.<sup>11</sup> This argument is closely connected to this thesis, and will be revisited in Xi Jinping's speeches regarding China's official visions for a more just and representative global economic governance in the upcoming methodology chapter.

However, this is not to suggest that China's efforts to establish the Bank have gone rather smoothly without any socialization process. On the contrary, establishing the Bank has indeed proved to be a mutual-shaping process involving socialization. From this point of view, Marcia Don Harpaz theoretically examines the coherence and variation in relation to China's behavior in trade, investment and development financing from both a rationalist and normative approach. With respect to the AIIB, she argues that a socialization process could be better to understand China's behavioral norm of establishing the AIIB in a sort of conforming yet challenging manner to the existing framework.<sup>12</sup> Similarly, Xiao Ren also highlights the fact that the AIIB's formation evidently presents a dynamic process of mutually shaping and being shaped, reflected by the intensive interaction between China's determined

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<sup>9</sup> Asian Infrastructure Investment Bank, 2015. *Asian Infrastructure Investment Bank Articles of Agreement*. [pdf] AIIB. Available at: <[https://www.aiib.org/en/about-aiib/basic-documents/\\_download/articles-of-agreement/basic\\_document\\_english-bank\\_articles\\_of\\_agreement.pdf](https://www.aiib.org/en/about-aiib/basic-documents/_download/articles-of-agreement/basic_document_english-bank_articles_of_agreement.pdf)> [Accessed 03 March 2017].

<sup>10</sup> Wang, Y., 2016. p.458.

<sup>11</sup> Chow, D., 2016. pp.1259-1264.

<sup>12</sup> Harpaz, M., 2016. China's Coherence in International Economic Governance. *Journal of Chinese Political Science*, 21(2), p.141.

efforts of shaping a potentially influential new institution, and China's refinement of the AIIB's role and assuagement of outside concerns and doubts, in regards to China's veto-power, good governance and standards, and accountability consistent with the existing multilateral banks.<sup>13</sup> In conclusion, though it entails a process of socialization of shaping and being shaped, the efforts taken by China in either way are sufficient and compelling enough to denote the fact that China has played a significant role in initiating and establishing the Bank. Given this reality, the role played by China in shaping the characteristic of the Bank's institutional design will be of value to be further explored and elaborated.

### *Internal Dimensions of the AIIB*

There are several important internal dimensions of the Bank that have been empirically examined. This strand of scholarship has offered some tentative but still thought-provoking entry points for further investigating the institutional design of the Bank in a more comprehensive and cohesive way.

Gregory Chin critically investigates how the AIIB represents both continuity and innovation with respect to global governance. More concretely with regards to the innovation aspect, the governance structures of AIIB and its overarching legal frameworks have constituted a novel foundation and prospect for unlocking the potentials for this newly established bank, to make innovative breakthroughs with respect to decision-making, management, staffing, and the lending practices and business models as well, and thus paving the way to give an adequate voice to emerging and developing countries.<sup>14</sup>

More concretely on a micro level, there are some scholarships paid to the AIIB membership. Kubalkova notes that the Bank is confronted by monumental challenges which are derived from institutional and financial accountability, and its capacity to live up to the promises of promoting economic cooperation and integration in the Asia-Pacific region, thus divergent membership which allows for well-diversified and well-balanced opinions in relation to the operating principles, in which enacted with democratic accord and accountability, should be pursued to hold China accountable

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<sup>13</sup> Ren, X., 2016. China as an institution-builder: the case of the AIIB. *Pacific Review*, 29(3), pp.438-40.

<sup>14</sup> Chin, G.T., 2016. Asian Infrastructure Investment Bank: Governance Innovation and Prospects. *Global Governance*, 22(1), p.12.

for its vows of increasing prosperity in the Asia-Pacific region, rather than creating a Chinese version of ‘golden straitjacket’.<sup>15</sup> In a similar fashion, Ming Wang argues that with the membership enlargement of the AIIB, an increasing pressure will be imposed on Beijing to follow the good extant international practices.<sup>16</sup> This strand of analysis, shedding light upon the membership trajectory and dynamics by pursuing inclusive membership, also entails a socialization process and thus provides insights for deepening the membership analysis in the forthcoming chapters. Acknowledging the importance of the membership issue, Mullen explores the various underlying determinants contributing to different countries’ divergent responses in terms of pursuing (or not pursuing) AIIB membership and notices that it is resulted from a complex and multifaceted interplay of geo-political and geo-economic interests, reflecting the competing and common interests in geography, domestic political economy, and institutional clout.<sup>17</sup> This analysis presents a very intriguing viewpoint in analyzing the uncommitted role played by U.S. in AIIB, when located in the context of U.S.-China rivalry.

### *Manifestation of Assertive and Normative China*

There are several interesting yet complementary framings about the move undertaken by China to initiate and establish the Bank. Among them, assertive China and normative china are more outspoken in this strand of thematic review.

#### *Framing 1: AIIB as an echo of assertive China*

The new leadership assumed power at the 18th National Congress of the Communist Party of China (CPC) in 2012 and the leadership transition was completed in the first session of the 12th National People’s Congress (NPC). After the transition, China’s new president Xi Jinping demonstrated a relatively proactive posture and was quickly presented as a powerful leader holding a strong vision and determination for achieving the great rejuvenation of the Chinese nation. Prompted by this vision, an apparent strategic transformation of China’s foreign strategy from *taoguangyanghui*

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<sup>15</sup> Kubalkova, P.G., 2015. Asian Infrastructure Investment Bank: New Asian Opportunity or China’s Hidden Strategy? *China Quarterly of International Strategic Studies*, 1(4), pp.667-85.

<sup>16</sup> Wan, M., 2016. Asian Infrastructure Investment Bank: The Construction of Power and the Struggle for the East Asian International Order. New York: Palgrave Macmillan.

<sup>17</sup> Mullen, A., 2016. Far East of Eden: Determinants of Membership in the Asian Infrastructure Investment Bank. Princeton University. Abstract only. Available at: <<http://dataspace.princeton.edu/jspui/handle/88435/dsp01xg94hs00z>> [Accessed 18 February 2017].

(keeping a low profile, KLP hereafter) to *fenfayouwei* (striving for achievement, SFA hereafter) was signaled.<sup>18</sup> Thus, China's construction of the Bank became a strong showcase of being proactive at a critical historical juncture through deploying the material and ideational resources at its disposal.

Following the ongoing debate of "Assertive China", Åberg re-conceptualizes Chinese assertiveness and connects it to the Chinese grand strategy of transformation. He further elaborates that the recreation of the AIIB is an evident example of Chinese assertiveness, anchored in grand strategy of target, cohesion and confidence, which stimulates China to SFA, unequivocally signifying China's status ascendance and aspiration by assuming leadership and responsibilities either regionally or globally, in despite of U.S. opposition.<sup>19</sup> While put differently, the Bank as a strategic power move by the rising China *vis-à-vis* the status quo superpower, is constructed on the basis of China's material and ideational resources, and considered as a self-evidently proactive symbol and historical trend, in which institutional development could be seen as a functional equivalent engendered by a mixture of interaction comprising convergent evolution, political lineage and power acquisition.<sup>20</sup>

An assertive China, in the context of U.S.-China rivalry, also attracts a lot of scholarly interest. Firstly, Chow argues that pushing forward the AIIB strongly displays Chinese' policy makers' frustration with the stalling tactics adopted by the U.S. in the reforms for a more just representation commensurate with its economic weight in the American-dominated Bretton Woods institutions.<sup>21</sup> While, Xiao Ren presents a dialectical perspective to consider the AIIB, politically and strategically, as an offensive initiative for being defensive, when China was confronted with U.S. Asia rebalance policy, hence going 'westward' to the vast Eurasian heartland and investing more resources bear more significant meaning for China's geopolitical and geo-economic status.<sup>22</sup> However, these two arguments are more prone to view the Bank in a zero-sum game created by China. Though situating the AIIB as one part of China's adjustment about its foreign policy especially related to U.S., differently,

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<sup>18</sup> Yan, X., 2014. From Keeping a Low Profile to Striving for Achievements. *Chinese Journal of International Politics*, 7(2), p.156.

<sup>19</sup> Åberg, J., 2016. A Struggle for Leadership Recognition: The AIIB, Reactive Chinese Assertiveness, and Regional Order. *Contemporary Chinese Political Economy and Strategic Relations: An International Journal*, 2(3), p.1132.

<sup>20</sup> Wan, M., 2016. pp.21-25.

<sup>21</sup> Chow, D., 2016. pp.1258-1260.

<sup>22</sup> Ren, X., 2016. p.436.

Yong Wang observes that Beijing has been constantly stressing the dialogue with U.S. on building a ‘new model’, namely, major country relations (新型大国关系) featured by no confrontation, no conflict and win-win situations. From this angle, he highlights that the Bank has presented both a challenge and an opportunity to the United States-China bilateral relations in the Asia-pacific region.<sup>23</sup>

From a rather U.S.-oriented perspective, Chow argues that the U.S.-perceived AIIB could potentially be utilized as a rival to the Bretton Woods institutions, concerning lending and rules of international trade in the advancement of its China’s global ambitions and goals, such as not in favor of the existing international best practices and policies embodied in Washington Consensus, and thus the AIIB marks a seismic economic power shift from the United States to China, and there will be growing competition regarding who will be the rule-writer for the international trade in the 21st century.<sup>24</sup> However, standing away from a static point of view, Glaser and Vitello have brought an updated observation on the U.S. evolving official discourse regarding the AIIB. They argue that thereafter witnessing the initial success of being supported by some of its strongest allies, the U.S. started to soften its rhetoric by proposing the possible collaboration between the AIIB and existing multilateral lenders like World Bank and ADB.<sup>25</sup>

In conclusion, locating the AIIB in the context of U.S.-China rivalry, emphases have been put on a mutual adjustment to each side’s policies and strategies. In this regard, the AIIB has created a double-side matter of fact, challenge-opportunity, assertive-defensive, and cautious-inclusive.

#### *Framing 2: AIIB as an echo of normative China*

The significant move taken by China to succeed in establishing the AIIB is viewed as a manifestation of China’s nascent normative power in the International financial governance landscape. In a nutshell, Peng and Tok have argued that the AIIB is a multi-functional platform, embodying Chinese norms such as non-interference, non-conditionality and infrastructure construction, which will enhance potential influence of social structures with Chinese characteristics in relation to the financial governance for promoting reforms in the IMF and World Bank, geared towards a

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<sup>23</sup> Wang, Y., 2016. p.461.

<sup>24</sup> Chow, D., 2016. p.1264.

<sup>25</sup> Glaser, B., Vitello, J., 2015. China Relations: China Makes Strides with AIIB and a Great Wall of Sand. *Comparative Connections: A Triannual E-Journal on East Asian Bilateral Relations*, 17(1), pp.25-26.

fairer representation of the developing countries and emerging economies.<sup>26</sup> From a broader perspective, Emilian Kavalski argues that China's normative power could be interpreted as the very antithesis to European Union (EU) type of cosmopolitanism through China's highlight on its 'singularly historical practice of universal principles that is open to emulation not as a universal pattern, but for its procedures in articulating the universal to concrete historical circumstances'. Put differently, China's normative power is premised on specific contexts, an intersection of discursive memories of the past combined with the contexts of the present and the prospective tasks of the future, rather than explicit norms of appropriateness.<sup>27</sup>

Another strand of normative China is demonstrated by Chinese multilateralism, as an underlying principle embedded in the AIIB. Through conducting a comparative analysis with American multilateralism, serving the U.S. as a hegemon to consolidate global leadership, Bin Gu concludes that Chinese multilateralism for the AIIB is characterized by its self-positioning in contributing to a complementary role in international development, tilting towards boosting a fairer representation and the voices of emerging economies and developing countries.<sup>28</sup>

In a similar fashion yet different approach, Callaghan and Hubbard's departure from the point of the Chinese multilateralism is intrinsically embedded in the AIIB, rather stressing that a fruitful exploration of the multilateralism in relation to the AIIB could be best situated in the context of its "One Belt One Road" strategy, in which we could examine the correlation between the establishment of a multilateral bank specially tailored to Asian infrastructure, and China's intention of de-politicizing the potentially fraught bilateral financing deals and boosting its positive image in the region. Therefore, he notices that the very necessity and importance for the AIIB to function as a truly multilateral institution, in accordance with the standards of other multilateral lenders, particularly safeguards, procurement and transparency.<sup>29</sup> This thematic review of normative China in relation to AIIB is of importance for understanding China's explicit and implicit role in shaping the characteristic of the

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<sup>26</sup> Peng, Z., Tok, S.K., 2016. The AIIB and China's Normative Power in International Financial Governance Structure. *Chinese Political Science Review*, Issues: Preprints, pp.1-3.

<sup>27</sup> Kavalski, E., 2013. The struggle for recognition of normative powers: Normative power Europe and normative power China in context. *Cooperation & Conflict*, 48(2), pp.252-59.

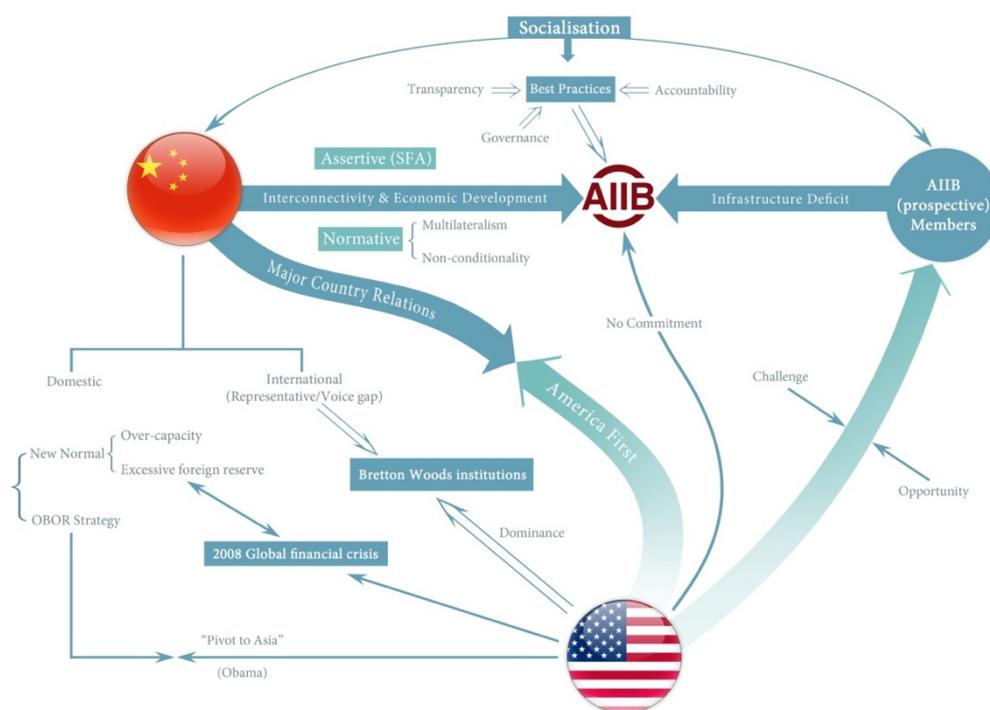
<sup>28</sup> Gu, B., 2017. Chinese Multilateralism in the AIIB. *Journal of International Economic Law*, 20(1), pp.137-158.

<sup>29</sup> Callaghan, M., Hubbard, P., 2016. The Asian Infrastructure Investment Bank: Multilateralism on the Silk Road. *China Economic Journal*, 9(2), pp.116-39.

Bank’s institutional design against the backdrop of Chinese official normative visions and appeals from Xi Jinping’s speeches, to further testify to what extent China’s normative appeals have been reflected in the institutional design itself.

To briefly conclude, after thematically and critically reviewing the relevant literatures, it is arguable that these three thematic strands of previous research are interconnected. As shown by figure 1, The underlying accounts, such as China's domestic political economy, dynamics of its external environment and perceived representation or voice gap, function as strong impetus for China to push the AIIB forward to a successful debut regionally and globally. During this process, China’s role also involves a process of socialization, in order to make the AIIB more transparent and accountable. Overall, China has played an assertive and normative role in creating the Bank, which is further testified by the embedded Chinese characteristics of multilateralism and non-conditionality in the Bank. This thematic literature review denotes a clear logic that China has explicitly and implicitly played a significant role in shaping the Bank, and thus lays a foundation for framing the two interconnected research questions and proceeding analysis.

**Figure 1. Summary of Previous Research**



Note: created by the author.

## **CHAPTER 2 METHODOLOGY AND RESEARCH DESIGN**

This chapter aims to elaborate and justify the methodological choices and methods applied in this thesis, and demonstrate that the applicability of the selected methods goes in accordance with the research aim of this thesis, therefore laying a solid foundation to proceed with the author's argument and provide clarification and transparency for the prospective reader.

### **2.1 Research Strategy and Research Design**

This thesis employs qualitative comparative design as the research strategy, due to its appropriateness in providing in-depth analysis and insight for investigating the characteristics of the Bank's institutional design, in contrast with IMF, World Bank and ADB. The key value of the comparative design approach is reflected in several aspects, such as taking the form of a multi-case study, especially in the field of organization studies. This plays a vital role regarding the understanding of causality, and allows the distinguishing of similar characteristics of different cases to serve as a stepping stone for theoretical reflection.<sup>30</sup> In this respect, this thesis also aspires to discover the interconnectedness of underlying accounts, and how they could contribute to the similarity and difference in the institutional design. This inquiry automatically connects to another research question of the thesis, to unveil the China's role in contributing to the Bank's institutional design against the backdrop of Chinese official visions and advocacy. After a systematic analysis, this thesis will apply the concept of bounded rationality to better reflect upon the rational institutional design theory.

#### ***Case selection:*** Why IMF, World Bank and ADB?

The goal of purposive sampling is to sample cases/participants in a strategic way, so that those sampled are relevant to the research questions that are being posed. Through a comparative design strategy, the IMF, World Bank and ADB are strategically selected on the basis of both theoretical sampling and generic purposive sampling. The two sampling approaches attempt to achieve both purposiveness and representativeness in relation to case sampling.<sup>31</sup> On one hand, the three selected

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<sup>30</sup> Bryman, A., 2012. *Social Research Methods*. 4th ed. New York: Oxford University Press. p.74.

<sup>31</sup> *Ibid.*, p.428.

cases, together with the AIIB fall into the theoretical toolkit formulated by the Rational Institutional Design theory. On another hand, the three cases are of critical significance due to the fact that they are the few iconic pillars of the existing international financial architecture, upholding governance, transparency and accountability and generating huge impacts to the international economic governance either in the Asia-Pacific region or worldwide.

## 2.2 Data Collection

In this thesis, documents and texts are utilized as the main sources of data, encompassing both the primary and secondary data sources in different but complementing functions in the data analysis.

With respect to institutional design, the primary data derived from the official publications, reports, and press releases from the concerning parties, including the AIIB, IMF, World Bank and ADB, is publicly available online through their official websites and databases. In relation to Chinese official visions for the Bank, the primary data is limited to the speeches of Xi Jinping, accessible at the Ministry of Foreign Affairs of the People's Republic of China. The official speeches are delimited to President Xi Jinping, due to the fact that Xi is the political figure most representative of China and his speeches could be seen as the prominent epitomes of the official Chinese standpoint. In addition, a spatial-temporal limitation of Xi's speeches has been applied as well. The spatial limitation exclusively lies in bilateral and multilateral diplomatic occasions, such as Indonesia's Parliament, APEC Summit, Bo'ao Forum, World Economic Forum, BRICS Summit, and G20 Summit. The temporal demarcation is limited to October 2013 onwards, in line with time of the Bank being officially announced.

As stressed by Bryman, researchers should take caution and review it as certain depiction of social realities, by virtue of their official and quasi-official characters.<sup>32</sup> Equally put, Atkinson and Coffey analyze that documents themselves exhibit a distinctive feature, referred as 'documentary reality'.<sup>33</sup> In this regard, we should be

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<sup>32</sup> Ibid., p.550.

<sup>33</sup> Atkinson, P., Coffey, A., 2011. Analyzing Documentary Realities, in: D. Silverman, ed. 2011. *Qualitative Research: Issues of Theory, Method and Practice*. London: SAGE, p79.

self-aware of specific socio-political and cultural contexts, in which the depiction of reality is generated. This also requires the researchers to attach self-awareness and sensitivity of the documents accessed, and this issue will be reexamined and addressed in the coming section of ethical considerations and self-reflexivity.

Last but not least, the secondary data extracted from the existing coverage of the research subject includes the previous research, social media coverage, and various reports and publications from think tanks. All the relevant secondary sources will be critically analyzed, to cross-check with the primary data, for the sake of mutually complementing and reinforcing the credibility and validity of the author's argument.

### **2.3 Data Analysis Method: Thematic Analysis**

Considering the two main research questions, this thesis will employ thematic analysis as the data analysis method to analyze the collected data. Thematic analysis moves beyond simply investigating the co-occurrence of particular explicit words or the incidence of particular phrases that are characteristic of particular writing genres, and focuses on identifying and describing both the explicit and implicit ideas within the data, namely, the themes.<sup>34</sup> This feature allows the flexibility of the themes to be identified either at a semantic level or at a latent level. Put differently, semantic theme attempts to identify the explicit meaning of the collected data through a rich description and representation of the data, whereas in contrast, latent theme give a resonance about the underlying ideas, norms, and assumptions through an insightful interpretation of the data.

As argued by Bryman, the thematic analysis is contested for not being identifiable, due to the facts that searching for particular themes is seen as a common activity that could be discerned in many other qualitative data analysis approaches and, for some writers a theme is seen as either too narrow like a code, or too broad, transcending everyone.<sup>35</sup> In this regard, a clear definition of theme and its relation with code should be put forward. Theme shall be considered as a category identified, usually built on the codes identified in the data, closely related to the research questions and providing a solid basis for the theoretical understanding of the data.<sup>36</sup>

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<sup>34</sup> Guest, G., MacQueen, K., Namey, E.E., 2012. *Applied Thematic Analysis*. London: SAGE. p.11.

<sup>35</sup> Bryman, 2012. p.578.

<sup>36</sup> *Ibid.*, p.580.

In this sense, we could argue that the code, given to particular pieces of the data, is a contributing building block for the particular theme. ‘*Framework*’, defined as a ‘matrix based method for ordering and synthesizing data’, is adopted as one practical strategy for assisting a thematic analysis, and helps to better construct themes and subthemes through a meticulous process of reading and rereading the data.<sup>37</sup>

The rationales for employing thematic analysis in this study lie in two main facets: 1) the flexibility of data analysis contingent upon different strands of data and research questions, and 2) its strong relevance and linkage to the main theoretical concepts outlined in rational institutional design. More specifically, thematic analysis will be used to analyze the related institutional documents, such as the AIIB Articles of Agreement, IBRD Articles of Agreement, Articles of Agreement of the International Monetary Fund, ADB Charter and their respective by-laws. Through the first lens, thematic analysis will be applied to comprehend the explicit meaning of the institutional documents as they are manifest, instead of interpreting the latent meanings, therefore respecting the neutrality of this strand of institutional-related data and avoiding intentionally biased comparisons in regards to the characteristic of the AIIB’s institutional design in parallel with IMF, World Bank and ADB in the forthcoming chapters. Through another lens, the thematic analysis will be critically employed to probe both the explicit and implicit meanings of the Chinese leaders’ speeches, and categorize them into different themes (and sub-themes) and underlying ideas or norms.

Specifically, this thesis will entail an attentive reading and appraisal of the original documents. For the AOA, it is rather clear and transparent to outline different categories such as *Purposes, Membership, Capital, Provisions, Operations, Organization & Management, Withdrawal & Suspension, and Immunities & Privileges*. These categories are seen as succinct codes initially, and are further theoretically integrated and constructed as themes, by drawing reference to the main analytical concepts employed by rational design on international organizations, Membership, Scope, Centralization and Control, in an approach of theoretical thematic analysis<sup>38</sup> recognized by David Grey, therefore generating the four analytical themes including ‘*Membership*’, ‘*Scope: Infrastructure Investment*’,

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<sup>37</sup> Ibid., p.579.

<sup>38</sup> Grey, D., 2014. *Doing Research in the Real World*. 3rd ed. Los Angeles, London: SAGE. pp.609-611.

‘Centralization’ and ‘Control: Voting Arrangement’. As for constructing the theme in Xi Jinping’s speeches, please see Table 1.

**Table 1. Theme Identification and Construction from Xi Jinping’s Speeches by Applying Thematic Analysis**

Data	Data	Theme Construction	
		Codes	Subthemes
<p><b>Topics</b></p> <p><b>Main data extracted from Xi Jinping’s Speeches</b></p> <p><b>Announcement:</b> AIIB will work together with the existing multilateral development banks in and outside the region and <b>complement</b> one another to fuel the sustained and steady growth of the Asian economy.  <b>* Function:</b> boost investment to support <b>infrastructure development</b> in Asia. It will serve to channel more resources, particularly private investment, into infrastructure projects to promote <b>regional connectivity</b> and <b>economic integration</b>.  <b>* Vision:</b>  1. function as a truly <b>international, rule-based and high-standard multilateral development bank</b>, learn from the experience and <b>best practices</b> of existing MDBs regarding governance structure, operation policy, safeguards and procurement policy, environment and social benefits and human resources management.  2. consistent with the evolving trend of the global economic landscape and will help make the global economic governance system more <b>just, equitable and effective</b>.  3. committed to open <b>regionalism</b>, and make the current multilateral system more dynamic, complement and facilitate common development of the existing multilateral institutions.  4. adapt itself to new trends in international development and accommodate the diverse <b>needs of developing members</b>.  <b>*China’s Role:</b>  1. Initiator: enabling China to undertake more <b>international obligations</b>, provide more international <b>public goods</b>, help bring mutual benefits and <b>win-win</b> outcomes to all side, and promote improvement of the current international economic system.  2. Supporter: Besides subscribing capital and special fund, China has the <b>confidence and capability</b> to ensure sustained and sound economic development and bring more opportunities and benefits to Asia and beyond.</p> <p>AIIB</p>	<p>Infrastructure development; Connectivity; Economic integration; Best practices; Regionalism; Multilateralism; International obligations; Public goods; Confidence and capacity; Opening-up</p>	<p>Economic development; Global governance; Balance of power; International obligation; Sovereignty; Non-intervention; The equality of peoples;</p>	<p>China’s Status: <b>A</b> <b>Reformist Revisionist</b></p>
<p>Global Governance</p> <p><b>Global economic governance</b> should be based on <b>equality</b>, better reflect the new realities of the world economic landscape, increase the <b>representation</b> and voice of emerging markets and developing countries and ensure that all countries have <b>equal rights, equal opportunities and equal rules</b> to follow in international economic cooperation;  Global economic governance should embrace <b>openness</b>, accommodating constructive suggestions, recommendations and <b>aspirations</b>, active <b>participation and integration</b> of various parties, rejecting exclusive arrangements and avoiding closed governance mechanisms and fragmentation of rules;  Countries need to step up communication and coordination, accommodate each other’s interests and concerns, and work together to discuss the rules, build mechanisms and meet challenges. Global economic governance should be a mechanism of <b>sharing</b>. It should be about participation by all and benefits for all.</p> <p>A community of shared future</p>	<p>Global governance; Representation; Equality; Win-win; Sharing</p> <p>Understanding; Sovereign Equality; Diversity</p>		

Source: Xi Jinping’s official speeches

As illustrated in Table 1, it is arguably reasonable to get a transparent outline of China's specific visions and its underlying social structures in relation to the Bank, in the context of Xi Jinping's official speeches.

Initially starting from the original context to final constructed theme, it is an attentive and self-reflexive process of familiarization with the data, outlining three highly relevant topics, including 'AIIB', '*Global Economic Governance*' and '*A Community of Shared Future*', and thereafter searching for preliminary, comprehensive and candidate codes to finally draw a systematic and coherent theme that constructively connects the explicit meaning in tandem with the underlying social structures. In this specific case, '*China's status*' was initially investigated and constructed as an overarching candidate theme. There are several crucial accounts contributing to that finding: 1) Xi Jinping actively emphasizes the initiative and constructive role played by China in proposing and founding the AIIB, manifested by its economic capacity and increasing confidence, indicating China both has the intent and capability of successfully engaging itself in a multilateral setting to voice its agenda; 2) Xi Jinping elaborates the importance and the necessity of pushing forward global economic governance, which should adhere to the principles and values of equality, openness, inclusiveness, efficiency and overall stability, while reflecting the new realities of the world economic architecture and in this sense, China should take the role of being a responsible country in fulfilling its international obligations; 3) Xi also entails certain ideational appeals, advocating for all countries' equal rights, equal opportunities and equal rules in the international economic sector, along with respect for sovereign-equality and cultural and political diversity and distinctiveness, in the framework of a common community of shared future for mankind. These three layers of observation denote a status-seeking agenda from China either economically or ideationally.

In a similar vein, Buzan has argued that China shares several paramount principles and values featured by a mixture of traditional Westphalian views of sovereignty and non-intervention, desire to preserve distinctive cultural values, top priority attached to regime security, and strong commitment to joint development through cooperation, trade and investment.<sup>39</sup> The further content of the identified

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<sup>39</sup> Buzan, B., 2010. China in International Society: Is 'Peaceful Rise' Possible? *The Chinese Journal of International Politics*, 3(1), p.14.

theme, a reformist revisionist,<sup>40</sup> is well-framed by Barry Buzan in the book of *People, States and Fear: National Security Problem in International Relations*. Drawing inspiration from Buzan's definition of reformist revisionist, which is closely related to the pluralist approach and only partly accepts some of the institutions of international society due to a mixture of calculated and instrumental reasons,<sup>41</sup> China's multi-attempts to accept, resist and reform the institutions of international society can be seen as a theme grounded in the original context of Xi's speeches. In the light of this, the candidate theme is therefore further revised as '*China's Status: A Reformist Revisionist*', to better explain the manifest and latent meanings of a dual construction: 1) a liberal and market-based stance on joint development, cooperation and interdependence in the economic sphere; and 2) adhering to sovereign equality and non-intervention as a means to preserve the uniqueness and diversity in cultural and political spheres.<sup>42</sup> This particular theme is also echoed by Qin Yaqing's argument that there is an intertwined co-constitution of continuity and change, basically, continuity through change in China's international strategy, illustrating that China's overall strategic design and policies are taking the course of continuity saturated with change, in line with its core national interests, including political security, economic development and sovereignty.<sup>43</sup>

In light of the aforementioned analysis, the theme '*China's Status: A Reformist Revisionist*' will provide a very valuable background knowledge to investigate and answer the second research question, specifically regarding non-conditionality and international character, and China's vision for democratizing the global economic governance.

## **2.4 Ethical considerations and self-reflexivity**

This thesis goes in accordance with the good research practices and ethical guidelines outlined by the Swedish Research Council and also draws a strong attachment to that formulated by Alan Bryman.<sup>44</sup> In this regard, this study aspires to eliminate the

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<sup>40</sup> Buzan, B., 1991. *People, States and Fear*. 2nd ed. London: Harvester Wheatsheaf. pp.237-46.

<sup>41</sup> Buzan, B., 2010. p. 18.

<sup>42</sup> Buzan, B., 2010. p. 31.

<sup>43</sup> Qin, Y.Q., 2014. Continuity through Change: Background Knowledge and China's International Strategy. *Chinese Journal of International Politics*, 7(3), pp.311-314.

<sup>44</sup> See Hermerén, G., 2011. *Good Research Practice*. Stockholm: The Swedish Research Council, and Bryman, A., 2012. *Social Research Methods*. 4th ed. New York: Oxford University Press.

possibility of incurring in any kind of ethical issue. Therefore, the data collection of the research has explicitly excluded interviews and field study, to a large extent, avoiding the common ethical issues faced by researchers employing these methods to conduct their research.

According to Bryman, self-reflexivity is an imperative element and should be exhibited to entail a sensitivity to the researcher's background in terms of political, cultural and social contexts, therefore being reflective upon the implications of applied methods, biases, values, and decisions for the knowledge generation.<sup>45</sup> In this regard, as a Chinese student studying the China-led AIIB, the author is well-aware of the homogeneity in value, culture and socio-politics and their according biases, and should be critical towards cultural native-ness and political biases. A crucial driver for conducting this research has been a critical investigation of the Bank's institutional design in comparison with the well-known multilateral financial institutions and how the AIIB could potentially evolve as a well-functioning and accountable MDB in the Asia-Pacific region.

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<sup>45</sup> Bryman, 2012. p.393.

## CHAPTER 3 RATIONAL INSTITUTIONAL DESIGN

This chapter introduces the relevant theories and concepts that are employed to analyze and interpret the data in the thesis. This thesis relies primarily on concepts of rational design in the context of international institutions. This chapter starts with a general introduction to rational design approach and thereafter elaborates upon the four dimensions of institutional design, encompassing membership, scope, centralization and control.

### 3.1 Introduction to rational design on international institution

In the past decade, scholarship of international institutions has attentively turned to rational design school in an effort to better understand and explain the ample diversity observed in the structures and rules that govern these institutions. In contrast with the realist and constructivist positions on international organizations, which either state that the international institutions are largely inconsequential shadows of state power, or view international institutions solely as exogenous actors exerting independent force through the normative power, the rational design school instead attempts to accept the assumption that international institutions are a manifestation yielded by the rational and purposive interactions among states and other international actors in order to solve specific problems.<sup>46</sup> Meanwhile, the work from Robert Keohane, *After Hegemony: Cooperation and Discord in the World Political Economy*, has offered an analysis of the efficiency reasons for reaching agreements among regime participants and seeks to illuminate that international organizations and institutions could be seen as means for states to overcome problems, including collective action, information deficits or asymmetries and high transactions costs.<sup>47</sup> This strand of argument largely displays the overall assumption of a rational choice approach that suggests agents are instrumentally rational and self-interested, acquire consistent preferences, maximize expected utility, and make decisions based on cost-benefit calculation (and/or strategic reasoning).<sup>48</sup> Following this logic, Coleman

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<sup>46</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. The Rational Design of International Institutions. *International Organization*, 55(4), p762.

<sup>47</sup> Keohane, R. O., 1984. *After Hegemony: Cooperation and Discord in the World Political Economy*. Princeton: Princeton University Press. pp.85-109.

<sup>48</sup> See Eriksson, L., 2011. *Rational Choice Theory: Potential and Limits*. Basingstoke: Palgrave Macmillan. p.17. and Martinez-Diaz, L., 2009. Boards of directors in international organizations: A framework for understanding the dilemmas of institutional design. *Review of International Organizations*, 4(4), p.384.

has provided a comprehensive but nuanced understanding to argue that the principal aim of the rational choice approach is to understand how actions that are reasonable or rational for actors can combine to generate social outcomes, encompassing the variance of both intention and unintention by actors, and both socially optimal and non-optimal.<sup>49</sup>

Drawing from the aforementioned, these insights provide a good theoretical angle to shed light upon underlying rationales and accounts contributing to China's choice of initiating and establishing the AIIB as a new MDB in the existing financial architecture at this juncture of time. Whereas, it's of importance to have a revisit and appraisal of actual outcomes and characteristics of the Bank's institutional design, to further probe whether the institutional design has achieved an optimal/non-optimal outcome contingent upon specific contexts and accounts.

Grounded in rational choice approach, Koremenos, Lipson and Snidal have conducted pioneering forays into explaining the rational design of international institutions, which further provide more critical and applicable theoretical toolkits to analyze the Bank's institutional design. To start with, Koremenos *et al.* define international institution as "explicit arrangements, negotiated among international actors that prescribe, proscribe and/or authorize behavior".<sup>50</sup> Five dimensions of institutional design encompassing membership rules (*Membership*), scope of issues covered (*Scope*), centralization of tasks (*Centralization*), rules for controlling the institution (*Control*), and flexibility of arrangements (*Flexibility*), functioning as lenses of investigating variance or similarity of different institutional designs.

Prior to comprehensively illustrating the varied dimensions of institutional design, some independent variables are identified beforehand, namely, distribution problems (*Distribution*); enforcement problems (*Enforcement*); number of actors and the asymmetries among them (*Number*); and uncertainty about behavior, the state of the world, and others' preferences (*Uncertainty*).<sup>51</sup> Meanwhile, a series of conjectures are particularly framed to connect independent and dependent variables

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<sup>49</sup> Coleman, J.S., Farraro, T.J. Introduction, in: J.S. Coleman and T.J. Farraro, ed.1992. *Rational Choice Theory: Advocacy and Critique*. California: SAGE. pp. ix-xxii.

<sup>50</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. p.763.

<sup>51</sup> *Ibid.*, pp.773-779. **Distribution problem** refers to selecting one outcome from a range of known possible outcomes; **Enforcement problem** refers to the strength of individual actors' incentives to cheat on a given agreement or set of rules; **Number of actors** refers to the actors that are potentially relevant to joint welfare because their actions affect others or others' actions affect them; **Uncertainty** encompasses the extent to which actors are not fully informed about others' behavior and preferences, and states' knowledge about the consequences of actions of their own, other states and international institutions.

outlined above, on the basis of four assumptions that are explicitly or implicitly drawn from rational choice approach.

*“Assumption 1 Rational design:* States and other international actors, acting out of self-interest, purposefully design institutions in the advancement of joint interests.

*Assumption 2 Shadow of the future:* The value of future gain is a strong incentive for a cooperative arrangement.

*Assumption 3 Transaction cost:* Establishing and participating in the international institutions is costly.

*Assumption 4 Risk-aversion:* States possess risk-averse characteristics and acknowledge the potential adverse effects upon creating or modifying the international institutions.”<sup>52</sup>

These four underlying and interconnected assumptions largely exhibit the overall assumption of rational choice in an agents’ volitional characteristics and capability to make decisions and act upon the basis of rational calculations of costs and benefits, as denoted by the core insights provided by Terry Moe, “economic organizations and institutions are explained in the same way: they are structures that emerge and take the specific form they do because they solve collective action problems and thereby facilitate gains from trade”,<sup>53</sup> which further illustrates that rational choice entails a process of consciously designing institutions, in which maximizing utility or minimizing cost have taken the forms of conscious design of institution, reducing transaction cost, being risk-averse, and shadow of future. When taking the variance of institutional design into consideration, Bobrow and Dryzek offered clarification by arguing “design is the creation of an actionable form to promote valued outcomes in a particular context”,<sup>54</sup> suggesting that the four assumptions above could contribute to variance of institutional designs that are contingent upon particular contexts.

### **3.2 Four analytical concepts embedded in rational institutional design**

In the light of the independent variables and key assumptions, four of the five dimensions of institutional design combined with their respective junctures which are of thematic theoretical importance central to the thesis, are attentively elaborated in

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<sup>52</sup> Ibid., pp.781-782.

<sup>53</sup> Moe, T.M., 1990. Political Institutions: The Neglected Side of the Story, *Journal of Law, Economics, and Organizations*. Special Issue, pp.217-18.

<sup>54</sup> Bobrow, D.B., Dryzek, J.S., 1987. Policy Analysis by Design. Pittsburgh: University of Pittsburgh. p.201.

this section. This thesis doesn't exhaustively include all the five dimensions as analytical concepts due to the fact that, while flexibility is significantly manifested by the Bank's preparatory stage, which involves "reflection upon the lessons from somewhere and a willingness to borrow those lessons where appropriate",<sup>55</sup> the flexibility of creating the Bank by drawing lessons and good practices from the existing international financial lenders is of more value to investigate the specific institutional arrangements inside the Bank.

### 3.2.1 Membership

Membership rules largely determine who enjoys the right to benefit and who pays the costs from an institution at the same time. Membership rules may work in several different ways, going beyond simply the reduction or enlargement of membership size. The members' homogeneity and asymmetry could be highly influenced by setting criteria for inclusion or exclusion, which may play a crucial role by way of generating various patterns of interactions and consequences.<sup>56</sup> Moreover, there are three conjectures attached to investigate the internal dynamics in advancing the analysis of membership.<sup>57</sup>

<b>Membership Conjectures</b>	Restrictive membership increases with the severity of the enforcement problem
	Restrictive membership increases with uncertainty about preferences
	Inclusive membership increases with severity of the distribution problem

Thus, the main conjectures in relation to membership could be summarized as follows: actors feel more incentive to join the club to enjoy the benefits of cooperation only confined to members. And membership could play a positive role for states to learn more about the preferences when certain actions, such as (un-)cooperation and (non-)compliance, could be clearly distinguished by the membership mechanism. Last, the expansion of membership will mediate distributional problems in the manner of extending possibilities for potential trade-offs amongst the members, which is also echoed by motivational complexity, one desirable principle of institutional design framed by Goodin, to denote 'goodness of fit' of accommodating the admixture of motives of different agents.<sup>58</sup>

<sup>55</sup> Goodin, R.E., 1996. Institutions and Their Design, in: R.E. Goodin, ed. 1996. *The Theory of Institutional Design*. Cambridge: Cambridge University Press, p.42.

<sup>56</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. p.770.

<sup>57</sup> Ibid., 783-784.

<sup>58</sup> Goodin, R.E., 1996. p.41.

### 3.2.2 Scope

In the context of rational institutional analysis, scope issue does not come as naturally pre-packed and well-defined units, instead it goes through the process of deliberate construction and gradual evolution, against the backdrop of states' deliberate choices to include or exclude certain issues in the institutional framework.<sup>59</sup> Notice that this is not simply to assert that the importance of the technological, cognitive-ideational, and other factors is not acknowledged here, by acquiring a more thorough understanding, this thesis refers to bounded rationality to offer a reflexive thought, embodying China's own cognitive constraints, and the complexities and underlying structures of environment, for acquiring a better understanding of the Bank's design outcome. Despite that, the scope dimension provides a good entry point to elaborate why certain issues are incorporated while others are not, and how different issues could produce different patterns of linkage within institutions. In this regard, scope conjectures concerning heterogeneity of actors, distribution and enforcement problems are presented.<sup>60</sup>

<b>Scope Conjectures</b>	Issue scope increases with greater heterogeneity among larger numbers of actors
	Issue scope increases with severity of distribution problem
	Issue scope increases with severity of enforcement problem

In conclusion, the scope conjectures suggest that the homogeneity of members will contribute to common vision, interests and position on certain limited issues, and *vice versa*, the heterogeneity within the group will possibly generate more diverse interests, alternatives and linkages for new scope issues or arrangements. In addition, the enforcement problem is closely related to the linkage and the incentives within and among issues. Another relevant principle of revisability is the embodiment of flexibility in the process of learning by doing and gradually evolving over the time,<sup>61</sup> which indicates the possibility of the gradual evolution of issue scope.

### 3.2.3 Centralization

It's worthy to clarify that centralization is not necessarily synonymous with centralized enforcement. There are more vital facets, such as centralization of

<sup>59</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. pp.770-771.

<sup>60</sup> Ibid.,785-786.

<sup>61</sup> March, J.G., and Olsen, J. P. 2006. The New Institutionalism: Organizational Factors in Political Life. *The American Political Science Review*, 100(4), p.745.

disseminating information, reduction of bargaining and transaction costs along with enhanced enforcement that could be embodied and taken into consideration of centralization lens.<sup>62</sup> There are four conjectures in relation to centralization as follows.<sup>63</sup>

<b>Centralization Conjectures</b>	Centralization increases with uncertainty about behavior
	Centralization increases with uncertainty about the state of the world
	Centralization increases with number
	Centralization increases with severity of the enforcement problem

In conclusion, the centralization conjectures suggest centralized information has the potential to offer an alternative for reducing the uncertainty about the behavior and increasing the efficiency of decentralized cooperation.<sup>64</sup> On a macro level, joint efforts of gathering and pooling information will be necessary to put forward among actors to ease the uncertainty in terms of the consequences of their actions in a global setting. To cope with the uncertainty about behavior, a Kantian-inspired publicity principle is framed by Goodin, to elaborate it as a litmus test to see whether institutions and institutional actions are publicly defensible.<sup>65</sup> With the increase of numbers of membership, centralization may play a positive role in reducing the transaction cost in terms of coordinating operational efforts and decision making.<sup>66</sup> Despite centralization's efforts to alleviate cooperation problems, largely aggravated by the uncertainty and number issues, enforcement problems still exist in the form of resorting to unilateral defection, rather than reciprocity-based cooperation. Therefore, centralization is further needed to exert more significant leverage to members within the institution.

### 3.2.4 Control

Acknowledging the characteristic of centralization, it is noteworthy to distinguish control from centralization since control and centralization do not necessarily entail a process of mutual influence. Investigation of control is more geared towards internal lenses. Considering this, Koremenos *et al.* have particularly emphasized voting

<sup>62</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. The Rational Design of International Institutions. in: B. Koremenos, C.Lipson, and D.Snidal, ed. 2001. *The Rational Design of International Institutions*. New York: Cambridge University Press, pp.11-12.

<sup>63</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. pp. 787-789.

<sup>64</sup> Axelrod, R., Keohane, R. O., 1986. Achieving Cooperation Under Anarchy: Strategies and Institutions. in: K. Oye ed.1986. *Cooperation Under Anarchy*. New Jersey: Princeton University Press, pp.226-54.

<sup>65</sup> Goodin, 1996. p.42.

<sup>66</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. p.788.

arrangements as one of the most observable and vital aspects of control.<sup>67</sup> Three conjectures regarding the individuality and asymmetry of control are presented below.<sup>68</sup>

<b>Control Conjectures</b>	Individual control decreases as number increases
	Asymmetry of control with asymmetry among contributors(number)
	Individual control increases with uncertainty about the state of the world

To conclude, it is arguable that with enlargement of membership, the leverage of individual members could be decreased for achieving collective consensus and benefits. Meanwhile, different members' contribution to the institution may vary a lot contingent upon their unbalanced capacities, thus more sway (asymmetry of control) will be presented in the voting arrangement.<sup>69</sup> In addition, members are risk-averse, and veto power is a special design feature to guarantee more protection in the face of uncertainty.<sup>70</sup>

**Figure 2. Relationships Between Independent Variables and Four Applicable Dimensions of Institutional Design Connected by Conjectures**

		Membership		Scope	Centralization	Control	
		Restrictive	Inclusive			Individual	Asymmetry
<b>Distribution</b>			↑↑	↑↑			
<b>Enforcement</b>		↑↑		↑↑	↑↑		
<b>Number</b>				*↑↑	↑↑	↓↓	◆↑
<b>Uncertainty</b>	Behavior				↑↑		
	The State of the world				↑↑	↑↑	
	Preferences	↑↑					
<b>Notes:</b>							
1. Number is categorized into three kinds: 1) number increase ↑, number decrease ↓; 2) heterogeneity increase *↑, homogeneity increase ※↑; 3) asymmetry of number ◆, symmetry of number “◇”							
2. Enforcement (severity increase ↑)							
3. Membership increase ↑							

Source: Koremenos, B., Lipson, C., Snidal, D., 2001. The Rational Design of International Institutions. *International Organization*, 55(4), pp.761-799.

<sup>67</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. p.12.

<sup>68</sup> Ibid., pp. 31-33.

<sup>69</sup> Koremenos, B., Lipson, C., Snidal, D., 2001. p.792.

<sup>70</sup> Ibid.

## CHAPTER 4 RATIONAL DESIGN OF THE ASIAN INFRASTRUCTURE INVESTMENT BANK(AIIB)

### 4.1 Rational design of the Asian Infrastructure Investment Bank(AIIB)

#### 4.1.1 Membership

The AIIB's membership is open to members of the World Bank(IBRD) or ADB. For applicants that are "not sovereign or not responsible for the conduct of its international relations, application for membership in the Bank shall be presented or agreed by the member of the Bank responsible for its international relations."<sup>71</sup> These membership rules in the AIIB present a '*change-through-continuity*' characteristic, a combination of continuity and change at the same time. In comparison with IMF and World Bank, whose memberships are strictly confined to "countries", the AIIB exhibits continuity in conforming to respecting '*sovereign countries*', while representing change in providing possible membership opportunities for a '*territorial entity*'. Compared with ADB, the Bank's continuity side is manifested by the possibility in nature for a non-sovereign entity to be a member while acknowledging the importance of sovereignty, while the change aspect is reflected by the scope of allowing that possibility of admission to membership. Specifically, that possibility in ADB is restrictively confined to the associate members of the United Nations Economic Commission for Asia and the Far East (UNECAFE),<sup>72</sup> such as 'Hong Kong, China', 'Macao, China', French Polynesia, etc. By contrast, AIIB doesn't exclude that possibility of admission to membership to any specific regional/international institution or agency, signifying its inclusiveness of going beyond the limitations of fixed geographical classification and institutional affiliation for applicants that are not sovereign or cannot hold responsibility for their conducts of international relations.

This special membership rule in the AIIB, presented through a change-through-continuity characteristic, has the potential to enlarge its membership diversity and heterogeneity, in the context of not only being restricted to countries, therefore providing a possible opportunity for a territorial entity to join AIIB,

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<sup>71</sup> AIIB, AOA, Article 3.

<sup>72</sup> ADB, AOA, Article 3, the name of United Nations Economic Commission for Asia and the Far East(UNECAFE) was officially changed as U.N. Economic and Social Commission for Asia and the Pacific(UNESCAP) in 1974.

although attached conditions in tandem with sovereign countries. Nevertheless, this change-through-continuity feature could also potentially, or already has, generated political tension and controversy, thus reflecting a hidden loophole in the institutional design of the Bank when practiced in practical political and economic context.

Taiwan, taken as an example, had officially presented the letter of intent to the AIIB preparatory committee for being considered as a prospective founding member of AIIB, but was rebuffed. The points of conflict are embodied in different interpretations of the membership rules enshrined in the Banks' Articles of Agreement (AOA). Ma Xiaoguang, the spokesman of the State Council Taiwan Affairs Office (SCTAO), reiterated that "through practical consultations, solutions will be found for Taiwan to join the bank with an appropriate identity...AIIB is an international multilateral development institution featuring openness and inclusion...Taiwan could join the AIIB despite failing to become a founding member."<sup>73</sup> This relatively soft and mediated official statement regarding Taiwan's possibility of joining AIIB actually unveils a long-standing political issue in the cross-strait relations, that is, the status/identity of Taiwan.<sup>74</sup>

Taiwan intended to apply for the AIIB membership according to the first clause of article three, "membership in the Bank shall be open to members of the International Bank for Reconstruction and Development or the Asian Development",<sup>75</sup> since Taiwan is an official member of ADB in the name of 'Taipei, China'. By contrast, from China's official stance, Taiwan's membership pathway for AIIB should be achieved under the third clause of the article three, especially road-mapping the prospective membership for those applicants who don't fall into the classification of sovereign countries. Tension and concern for this issue was straightforwardly expressed in the remarks delivered by Hua Chunying, spokeswoman of Ministry of Foreign Affairs (MFA), "as for Taiwan joining the AIIB, we maintain that we should avoid the 'two Chinas' and 'one China, one Taiwan'

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<sup>73</sup> SCTAO, 2016. *Mainland to consider all-around opinions on Taiwan's identity in AIIB*. [online] Available at: <[http://www.gwytb.gov.cn/xwfbh/201504/t20150415\\_9584523.htm](http://www.gwytb.gov.cn/xwfbh/201504/t20150415_9584523.htm)> [Accessed 15 March 2017].

<sup>74</sup> Taiwan is not a member of the IMF or the World Bank due to Chinese objections, but it is included in APEC (because APEC is defined as a grouping of Pacific economies rather than countries.) Unless the AIIB members are defined using similar language, Taiwan's participation won't get off the ground. The International Olympic Committee refers to it as '*Chinese Taipei*', and it is known as the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu at the World Trade Organization. It is a member of the ADB under the name 'Taipei, China', while officially the government refers to itself as the Republic of China.

<sup>75</sup> AIIB, AOA, Article 3.

situation.”<sup>76</sup> Therefore, China’s official line stood in contrast with Taiwan’s, characterized by its attempt to participate in the international organizations under the name Taiwan or Republic of China(ROC), or ‘Chinese Taipei’ as the bottom line. Officials of Taiwan clearly stated that Taiwan should be treated with equality and dignity, and would not accept the arrangement of applying for AIIB membership through China’s Ministry of Finance(MOF).<sup>77</sup> This underlying conflict point actually reveals that the Bank’s membership design is not only a financial platform of addressing economic issues, but also an arena of exerting politics, power and leverage.

The change-through-continuity characteristic is also presented by the nuance in defining ‘region’ or regional members, especially in relation to AIIB and ADB, since they are self-positioned as regional multilateral development bank (MDBs). For AIIB, the term ‘region’ and ‘Asia’ is expected to comprise the geographical regions and composition classified as Asia and Oceania by the U.N., while the term ‘region’ for ADB draws reference to the UNECAFE. This definition difference is further reflected in the membership classification. Take Turkey for example, which falls into the category of regional member in AIIB but non-regional member in ADB. Considering the definition difference, it may generate a long-term ramification for the membership of AIIB, which takes a rather broadly-embracing approach to attract more countries that potentially entail geographical attachment to joining a ‘regional membership’ club. This gesture may also potentially broaden the investment scope within the region, thus gradually increasing the economic homogeneity regarding the same pursuit of infrastructure investment and economic cooperation, in parallel with China’s OBOR strategy.

At this juncture of time, AIIB’s position itself is as a regional financial lender, thus its reach and influence fall short in comparison with IMF and World Bank. However, this doesn’t carry a pessimistic tone for its potential development. Another interesting aspect to note, as showed by Map 1, is that the distribution of AIIB’s

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<sup>76</sup> MFA, 2015. *Foreign Ministry Spokesperson Hua Chunying’s Remarks*. [online] Available at: <[http://www.fmprc.gov.cn/web/wjdt\\_674879/fyrbt\\_674889/t1251150.shtml](http://www.fmprc.gov.cn/web/wjdt_674879/fyrbt_674889/t1251150.shtml)> [Accessed 15 March 2017].

<sup>77</sup> See Taiwan rejects joining AIIB under China’s supervision, *Taipei Times*, [online] 14 April 2015. Available at: <<http://www.taipetimes.com/News/front/archives/2015/04/14/2003615878>> [Accessed 12 April 2017].  
Cheng, T. F., 2016. Taiwan rejects joining AIIB under China’s supervision, *Nikkei Asian Review*, [online] 13 April 2015. Available at: <<http://asia.nikkei.com/Politics-Economy/International-Relations/Taiwan-rejects-joining-AIIB-under-China-s-supervision>> [Accessed 12 April 2017].

membership is quite broad compared with the more Asia-Pacific oriented ADB, with its gravity of membership adjacent to Eurasian heartland.<sup>78</sup> Meanwhile, AIIB's membership showcases the diversity and heterogeneity of bodies represented, implying the chance of taking a gradual path of advancing the Bank from being regional-oriented, ultimately towards a cross-regional institution with international forward-looking vision and clout. The current membership also demonstrates that AIIB has taken a rather inclusive stance to absorb prospective members. In consideration of these facts, some attention should thus be diverted to the distribution problem along with the increasingly diverse or competing preferences and expectations from members. Therefore, the reliability and efficiency of the membership rules will be largely premised on the ongoing and forthcoming operation of the Bank to further coordinate and integrate the according demands and practical projects into a unified force for fulfilling the promises of the Bank.

**Map 1. AIIB Membership**



Source: AIIB; Perry-Castañeda Library Map Collection, University of Texas at Austin.

#### **4.1.2 Scope: Infrastructure Investment**

The issue scope of AIIB is clearly confined in its founding documents which set out the specific purposes and functions for which the Bank was established. According to

<sup>78</sup> Wan, M., 2016. p.76.

Article 1 of its AOA, the purposes of the Bank include the advancement of sustainable development, wealth creation and improvement of infrastructure connectivity in Asia, promotion of regional cooperation and partnership through collaborating with other development institutions.<sup>79</sup> More concretely, to implement these purposes, the Bank is expected to provide sovereign and non-sovereign finance for developing sound and sustainable projects in infrastructure and other productive sectors, including rural infrastructure and agriculture development, energy and power, environmental protection, transportation and telecommunications, water supply and sanitation, urban development and logistics.”<sup>80</sup> Notably, there is a commonly prevalent practice in the Fund, World Bank and ADB, namely, these international institutions have gradually extended their issue scope, and performed a range of tasks that were not foreseen at the time of their establishment, therefore their respective roles have been gradually changing and adapting as time evolves. Put differently, though circumscribing the explicit goals to a few well-defined issues in their founding documents, their issue scopes have been gradually adapting to new circumstances and incorporating new issues in the old framework, and inevitably there exists a certain spectrum of deviation from its original mandate and purposes.

Taking World Bank for example, the IBRD’s AOA straightforwardly outlines five purposes, namely, assisting reconstruction and development, fostering private foreign investment, promoting balanced growth of trade, arranging loans for more useful and urgent projects, and bringing about a smooth transition from a wartime to a peacetime economy.<sup>81</sup> However, the purpose and issue scope of World Bank seems to be geared more towards alleviating poverty through the supply of technical and financial support, thus progressively expanding from the original mandate to encompass new areas and issue scopes.<sup>82</sup> This evolution of the issue scope of the World Bank has been criticized constantly for its ‘mission creep’ by expanding towards issues and agendas such as biodiversity and corruption, in the pursuit of

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<sup>79</sup> AIIB, AOA, Article 1.

<sup>80</sup> Asian Infrastructure Investment Bank(AIIB), 2017. Our Work. [online] Available at: <<https://www.aiib.org/en/about-aiib/who-we-are/our-work/index.html>> [Accessed 12 January 2017].

<sup>81</sup> International Bank for Reconstruction and Development, 2012. *International Bank for Reconstruction and Development Articles of Agreement*. [pdf] IBRD. Available at: <[http://siteresources.worldbank.org/EXTABOUTUS/Resources/IBRDArticlesOfAgreement\\_links.pdf](http://siteresources.worldbank.org/EXTABOUTUS/Resources/IBRDArticlesOfAgreement_links.pdf)> [Accessed 05 March 2017].

<sup>82</sup> Wounters, J., Odermatt, J., 2014. Comparing the Four Pillars of Global Economic Governance: A Critical Analysis of the Institutional Design of the FSB, IMF, World Bank, and WTO. *Journal of International Economic Law*, 17(1), p.58.

incrementally democratic and humanistic agendas without appearing to be politically intrusive.<sup>83</sup> In light of the fact that many organizations have experienced a natural evolution over time, the Bank's scope through highlighting infrastructure as its core mission, demonstrated by its preamble and objectives in the AOA, seems to be a practical entry point to make the Bank operative without covering a systematically grand agenda like World Bank, particularly at the Bank's initial stage of development.

Besides the rationale of smoothly and efficiently running the Bank with its limited issue scope, there is another question of significance to be raised; why infrastructure investment in particular? As indicated by the previous research, there are some paramount, pragmatic and reasonable factors standing out to be articulated for setting up the infrastructure investment as the focal point of the Bank.

To begin with, there is a widely held consensus to accommodate the fact that infrastructure development plays a vital role in promoting economic growth and social development and there is indeed an infrastructure investment deficit in Asia.

In the light of this reality, the establishment of the Bank, functioning as a multilateral financial institution on infrastructure development, will largely mobilize the resources to deal with the financing bottlenecks and infrastructure deficit. This argument is highly proven to be appropriate and logical by the consistency of the ADB reports. In 2009, ADB and the ADB Institute had projected infrastructure needs for developing Asia from 2010 to 2020 in the report of *Infrastructure for a Seamless Asia*, covering thirty-two of ADB's forty-five developing member countries in relation to four infrastructure sectors, namely, transport, power, telecommunications, and water supply and sanitation. At the foremost, this comprehensive report projected that total investment needs for the infrastructure sectors was estimated to reach slightly above \$8 trillion over the next eleven-year period, almost \$750 billion a year.<sup>84</sup> The new report *Meeting Asia's Infrastructure Needs* published in 2017, has updated these estimates on the basis of the 2009 version, and two sets of infrastructure investment needs are presented: 1) Taking into account the costs of mitigation and adaption, developing Asia will need to invest \$26 trillion over the fifteen-years from 2016 to 2030, almost \$1.7 trillion per year; and 2) Removing climate-adjusted costs,

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<sup>83</sup> Einhorn, J., 2001. The World Bank's Mission Creep. *Foreign Affairs*, 80(5), p.24.

<sup>84</sup> Asian Development Bank, 2009. *Infrastructure for a Seamless Asia*. [pdf] ADB. Available at: <<http://adb.org/sites/default/files/pub/2009/2009.08.31.book.infrastructure.seamless.asia.pdf>> [Accessed 25 March 2017].

the infrastructure needs will amount to \$22.6 trillion, almost \$1.5 trillion per year.<sup>85</sup>

Under the dome of this known fact, this infrastructure investment deficit has marked a contrast with China's economy situation during the aftermath of the 2008 global financial crisis. China's growth has decelerated due to the global financial crisis of 2008. As a counter-crisis solution, the Chinese central government has resorted to the expansion of public investment, amounting to CNY4 trillion, and easing monetary policy. This policy has generated side effects; scilicet domestic over-investment, excess capacity and excess credit. Among them, excess capacity has been massive, thus standing out even measured by Chinese standards, especially in the infrastructure productive sectors including steel and cement.<sup>86</sup> Since Xi assuming leadership, China has officially admitted its entry into a new normal of Chinese economy,<sup>87</sup> as a response, in-depth structural reforms have to be embarked upon to reduce the over-investment, excess capacity and excess credit problems to aim for a relatively balanced, and sustainable economic growth.<sup>88</sup>

At this critical juncture in time, expanding the external demand, through AIIB's operation as the financial pillar situated in China's grand OBOR strategy, may be utilized as a sensible and pragmatic outlet to further integrate the domestic dynamics and external infrastructure demands for the sake of deepening domestic market-oriented reform. This provides economic stimulus for infrastructure enterprises going global, optimally utilizing the industrial overcapacity and excessive foreign exchange reserve, while at the same time accommodating the infrastructure demands in the Asian developing economies.<sup>89</sup> This outlet is also proven to be doable and appropriate in line with Chinese development lessons, setting infrastructure building as a top priority and foundation for the national economic growth. Nevertheless, it's impossible to depict an exhaustive picture of the multi-layered rationales for limiting the issue scope to infrastructure investment, but it still sheds

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<sup>85</sup> Asian Development Bank, 2017. *Meeting Asia's Infrastructure Needs. Agreement of Establishing the Asian Development Bank*. [pdf] ADB. Available at: <<https://www.adb.org/sites/default/files/publication/227496/special-report-infrastructure.pdf>> [Accessed 25 March 2017].

<sup>86</sup> Kawai, M., 2015. Asian Infrastructure Investment Bank in the Evolving International Financial Order. in: D. Bob ed. 2015. *Asian Infrastructure Investment Bank: China as Responsible Shareholder?* Available at: <[https://spfusa.org/wp-content/uploads/2015/07/AIIB-Report\\_4web.pdf](https://spfusa.org/wp-content/uploads/2015/07/AIIB-Report_4web.pdf)> [Accessed 19 March 2017].

<sup>87</sup> 'New Normal' is a concept used by Chinese leaders and economists to describe the ongoing slowing down of growth to around 7.0 percent GDP a year as well as the forbidden tasks of transforming the growth model from one driven by exports and investment toward one driven by domestic consumption.

<sup>88</sup> Kawai, M., 2015. p.13.

<sup>89</sup> Wan, M., 2016. p.54.

light upon the issue by offering a logical demand-supply analysis against the backdrop the mutual dynamics of Chinese domestic economy and the greater regional economic landscape.

There is another important question concerning the future expansion of the issue scope of the Bank which is also an intriguing thing to be tentatively reflected upon. Is it likely the AIIB will take the same development path of World Bank and ADB to incorporate more dimensions of social development, going beyond simply financing the real economy in infrastructure and productive sectors? The outlook still remains unclear at the moment, whereas at least, it's optimistic to argue that the resilience of the Bank's continuous support for infrastructure development and enhanced interconnectivity in Asia will not get stagnated in a purely economic dimension, due to the fact that the Bank has established its own Environmental and Social Framework (ESF) to better achieve environmentally and socially sustainable development outcomes. More specifically, the Bank has acknowledged the significance of social development and inclusion, for sound development.<sup>90</sup> It's also notable that social development and inclusion, in the sense of empowering people with equity of opportunity to participate in and benefit from the development process, are in a manner consistent with and contingent upon local conditions.<sup>91</sup> This statement actually leaves ample room for contestation and different interpretations regarding what the explicit indicative criteria of social development and inclusion outlined in the Bank are.

In light of the aforementioned, the issue scope of the Bank remains very much 'a work in progress'. At its initial stage of development, the Bank will be likely to solely focus on infrastructure investment while acknowledging the importance of environmental and social sustainability, social development and inclusion, by virtue of the fact that the current homogeneity of members in the context of facing daunting infrastructure demands, creating mutual economic interests and sharing common visions for cooperation and development. This current issue scope will be likely to be broadened or deepened when future conjectures arise to increase the heterogeneity of the membership along with the pursuit of more diverse interests and agendas, which

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<sup>90</sup> Asian Infrastructure Investment Bank, 2015. *Environmental and Social Framework*. [pdf] AIIB. Available at: <[https://www.aiib.org/en/policies-strategies/\\_download/environment-framework/20160226043633542.pdf](https://www.aiib.org/en/policies-strategies/_download/environment-framework/20160226043633542.pdf)> [Accessed 17 March 2017].

<sup>91</sup> Ibid.

could potentially generate more leverage and linkage to invite new issues or arrangements in.

### **4.1.3 Centralization**

In order to probe the centralization issue, it is vital to revisit the organization and management in the AOA, since it contains most of the transparent information regarding elements of centralization, such as reduction of bargaining and transaction costs and enhanced enforcement.

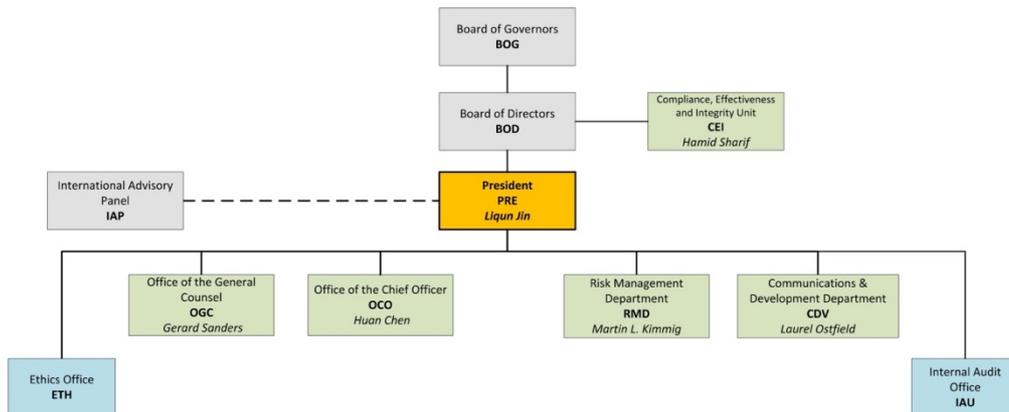
The change-through-continuity characteristic is exhibited by the organizational structure of AIIB. Compared with the Fund, World Bank and ADB, the Bank also adopts a similar governance structure as illustrated by Figure 3, composed of three layers of structure, namely a Board of Governors, a Board of Directors and the President and bank management team. More specifically, the highest decision-making body under the Articles of Agreement lies in the Board of Governors, where all the powers of the Bank are vested, consisting of one governor and one alternative governor who shall be appointed by each member country. The Board of Directors is responsible for the general direction of the operations of the Bank; exercising all the powers that have been delegated by the Board of Governors, encompassing approval of the Bank's strategy, annual plan and budget, establishment of policies, decision-making regarding operations of the Bank, supervision of the management and operation of the Bank.<sup>92</sup> According to the AOA, the Board of Directors is composed of twelve members, among whom there are nine elected by regional members and three elected by non-regional members.<sup>93</sup> Furthermore, the distribution of regional and non-regional directors is anchored in a constituency system, which is commonly used for the representation of members in virtually similar ways among the Fund, World Bank and ADB.

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<sup>92</sup> Asian Infrastructure Investment Bank(AIIB), 2017. Governance [online] Available at: <<https://www.aiib.org/en/about-aiib/governance/index.html#structure>> [Accessed 22 January 2017].

<sup>93</sup> AIIB, AOA, Article 25.

**Figure 3. Organizational Structure of AIIB**



Source: AIIB

Although AIIB has largely followed this typical organizational structure, commonly adopted by MDBs, the Bank also presents certain spectrum of change. Firstly, the board of directors of the Bank seems to have more limited power than those of the Fund, World Bank and ADB, since it will “function on a non-resident basis except as otherwise decided by the Board of Governors by a super majority vote”.<sup>94</sup> Compared with the Fund, World Bank, and ADB, the most influential member states, such as the U.S. and Japan, are represented by their respective resident executive directors in the executive board (or Board of Directors), which provides a platform for the executive directors’ active involvement in terms of voting on new policies, major programs and project decisions on a day-to-day basis. The in-residence board directors may also generate important leverage towards the management and the lending decisions of the institution as well. The rationale for a non-resident board in AIIB is to strive for cutting costs, improving efficiency, and streamlining the decision-making processes that have been often slowed down by the resident boards, which usually produce a certain level of confusion and tension with the management over day-to-day operations, and further plays a negative part in its due role in strategic direction and overall performance within an institution.<sup>95</sup> This arrangement is also seen as contestable, potentially weakening the role of the major shareholders at AIIB and thereby largely strengthening the power of the Bank’s management. Furthermore, the operations and loan decisions of the Bank are likely to

<sup>94</sup> AIIB, AOA, Article 27.

<sup>95</sup> Chin, G.T., 2016. p.16.

be largely influenced by China, who is the dominant shareholder and country of origin for the first president, and possesses the venue for the bank's headquarters, thereby playing a multi-functional role in the Bank. In this sense, the non-resident board is considered to be a purposive vehicle for advancing China's interests.<sup>96</sup> This contestation about the non-resident board actually reveals a commonly held belief in China and other developing countries that a leaner AIIB could be a good trial for accommodating both good safeguards and efficiency by drawing lessons from the existing MDBs. This particular arrangement actually echoes one statement of Zedillo's Report, titled *Repowering the World Bank for the 21st Century*, "delegation would also increase accountability by eliminating the conflict of interest inherent in the Board's co-managerial role and by placing responsibility for financing operations unambiguously on the shoulders of Management."<sup>97</sup> This further reveals a pervasive and confusing abundance of co-managerial practice roles by the resident board, which is argued to have been attempting to function an 'impossible trinity' of roles, embodying the representation of the interests of member nations, fulfilment of responsibility for bank policy, and provision of oversight of those same policies.<sup>98</sup>

Viewing from a macro level, the arrangement of the non-resident board highly reflects the co-constitution of centralization and de-centralization. For the de-centralization side, the non-resident board has clearly defined the due roles of the Board of Governors, Board of Directors, and Management under the AOA. This settlement presents a well-defined hierarchical organizational structure with clear division of duty to carry out, thereby further avoiding the duty confusion and overlapping operations. In this regard, this arrangement contributes to the overall de-centralization of the institution even though the organizational structure is hierarchically constructed. Viewing from the micro level of management, this arrangement undoubtedly has strengthened its autonomy and centralization of accelerating decision-making in terms of proposing loans and investment decisions, and prompting the efficiency of implementing the approved projects.

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<sup>96</sup> Kawai, M., 2015. pp.7-15.

<sup>97</sup> International Bank for Reconstruction and Development, 2009. *Repowering the World Bank for the 21<sup>st</sup> Century*. [pdf] IBRD. Available at: <<http://siteresources.worldbank.org/NEWS/Resources/WBGovernanceCOMMISSIONREPORT.pdf>> [Accessed 12 April 2017].

<sup>98</sup> Center for Global Development, 2009. *Zedillo Report Sparks Fresh Push for World Bank Reform*. [online] Available at: <<https://www.cgdev.org/article/zedillo-report-sparks-fresh-push-world-bank-reform>> [Accessed 12 April 2017].

In addition, adopting a non-resident board also plays a positive role in reducing operating costs. David Dollar has offered a critique towards the resident board and its financial cost to the World Bank, arguing that an extra layer of management has slowed down project preparation and reduced the efficiency of the bank, with an operational cost amounting to \$70 million annually.<sup>99</sup> Conversely, this amount will be saved with the assistance of modern communications technology, as stated in Article 27(4), “The Board of Directors shall establish procedures whereby the Board can hold an electronic meeting or vote on a matter without holding a meeting.”<sup>100</sup> This electronic countermeasure aims for mitigating the potential downside of rationally designing the Bank with a non-resident board, therefore ensuring the effective oversight of the institution in a much leaner way. The reduction of costs also has been exhibited in regulating that there is no remuneration for the governors and alternative governors except some reasonable expenses incurred attending meetings.<sup>101</sup> This clause of the Bank goes exactly in accordance with those in the Fund, World Bank and ADB, displaying the continuity characteristic from another angle. Reducing the bargaining, transaction and operational costs to its fullest forms has largely reflected that AIIB thus has displayed an incremental tendency towards centralization in running the Bank in the manner of being efficient and lean.

Last but not least, it’s of importance to offer a reflective thought on why AIIB has generally exhibited a tendency of centralization. At the outmost, the centralization is largely to do with the heterogeneity and uncertainty of AIIB members. Though the membership size of the Fund and World Bank is much larger than that of AIIB, it doesn’t mean the Bank’s potential hindrance is less limited, on the contrary, the Bank will encounter enormous challenges since the infrastructure demands will be vast from Asian developing countries, some of which are frustrated with the conditionality attached to demanding painful restructuring measures embodied by Washington Consensus from the existing MDBs that are largely driven by risk-averseness. In this regard, AIIB will confront more infrastructure demands along with the pursuit of less or no strings attached. For the sake of the Bank’s accountability, economic benefits and long-term survival, leaning towards centralization will prompt the Bank to

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<sup>99</sup> Dollar, D., 2015. Lessons for the AIIB from the Experience of the World Bank, *Brookings*, [online] 27 April 2015. Available at: <<https://www.brookings.edu/articles/china-on-the-global-stage/>> [Accessed 18 April 2017].

<sup>100</sup> AIIB, AOA, Article 27.

<sup>101</sup> AIIB, AOA, Article 22.

facilitate the efficiency of decision-making concerning proposing programs, issuing loans and implementing projects, thus effectively monitoring and mitigating the potential downsides of infrastructure projects with less attached conditions.

In addition, this centralization tendency could be interpreted as a shadow of China's political economy when it is placed on a multilateral setting. According to the Chinese official view on AIIB, adopting the best practices from the existing MDBs does not mean excluding unique legacies or experiences from China's own development path and its political economy. To some extent, the creation and operation of AIIB reveals an unforeseen and contestable connection with China's official assistance, and its authoritarian rule in the domestic governance. "China's development planning has been heavily influenced by the political priority of securing the CPC's grip on power."<sup>102</sup> The domestic logic of authoritarian rule and developmental thinking has generated certain leverage towards the Bank, on account of China being the initiator and the dominate shareholder in the Bank. More centralization at the management level could be utilized as a useful instrument to advance its latent agendas with grip on maneuverability, stability and control, though under the well-articulated framework of win-win cooperation.

#### **4.1.4 Control-Voting Arrangement**

In many international organizations such as the U.N., 'one country, one vote' rule typically represents the principle of sovereign equality of states. By contrast, in global economic governance, for MDBs, weighted voting is typically adopted to account for their relative economic size and the power of their members, allowing the countries of economic importance to have greater representation in the organization.<sup>103</sup> The change-through-continuity characteristic is also applicable to the voting arrangement in AIIB, since it also adopts the weighted voting as its electoral system, despite a slight difference in formulas compared with those of the Fund, World Bank and ADB.

With respect to the Bank, the allocation of voting powers among different member countries is basically determined by the allocation of capital subscriptions. As Article 4 states, the authorized capital stock of the Bank is one hundred billion

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<sup>102</sup> Heep, S., 2014. *China in Global Finance: Domestic Financial Repression and International Financial Power*. Cham: Springer International Publishing. p.14.

<sup>103</sup> Weighted voting is characterized an electoral system in which not all voters have the same amount of influence over the outcome of an election. There are different names of weighted-votes contingent upon different organizations, such as, the Fund uses quota-based votes, World Bank adopts share votes, while ADB applies proportional votes.

United States dollars, which is divided into one million shares having a par value of 100,000 dollars each.<sup>104</sup>

AIIB’s allocation of capital subscriptions across member countries is determined by Gross Domestic Product (GDP). A combination of current U.S.-dollar GDP (converted at market exchange rates) and current international-dollar GDP (converted at purchasing power parity rates) is used for calculating the economic size of individual members, according capital subscriptions and voting powers. More specifically, a 60% weight is assigned to current U.S.-dollar GDP and a 40% weight to current international-dollar GDP. In light of this calculation, there is another clear demarcation of total subscribed capital stock by regional members and non-regional members, as well-stipulated by Article 5, “no such subscription shall be authorized which would have the effect of reducing the percentage of capital stock held by regional members below seventy-five percent of the total subscribed capital stock, unless otherwise agreed by the Board of Governors by a Super Majority vote.”<sup>105</sup> This 75 percent of subscribed capital stock by regional members in AIIB is 15 percent higher than that of ADB, stated in a similar fashion, “no such subscription shall be authorized which would have the effect of reducing the percentage of capital stock held by regional members below sixty (60) per cent of the total subscribed capital stock.”<sup>106</sup> From this design difference, in contrast with ADB, who limits the shares of non-regional members not above one-quarter, the AIIB apparently aims to preserve the representation and influence of the Asian regional members states in the bank, at least for the initial stage of the Bank’s development.<sup>107</sup>

**Table 2. Composition of Voting Power in AIIB, IMF, IBRD, and ADB**

	Voting power	Notes
<b>AIIB</b>	basic votes + share votes + founding member votes	basic votes = $\frac{12\% \text{ aggregate sum of votes}}{\text{number of membership}}$ founding members votes=600 votes
<b>IMF</b>	basic votes + quota-based votes	basic votes = $\frac{5.502\% \text{ aggregate sum of votes}}{\text{number of membership}}$
<b>IBRD</b>	basic votes + share votes	basic votes = $\frac{5.55\% \text{ aggregate sum of votes}}{\text{number of membership}}$
<b>ADB</b>	basic votes + proportional votes	basic votes = $\frac{20\% \text{ aggregate sum of votes}}{\text{number of membership}}$

<sup>104</sup> AIIB, AOA, Article 4.

<sup>105</sup> AIIB, AOA, Article 5.

<sup>106</sup> ADB, Charter, Article 5.

<sup>107</sup> Chin, G.T., 2016. p.14

Source: AOAs of AIIB, IMF, IBRD and ADB.

In view of the composition and formula of the voting power, we could largely see the Bank's continuity in line with the Fund, World Bank and ADB, adopting a similar voting formula which encompasses the basic votes and share votes, where the salient changes are reflected by the percentage of basic votes in the aggregate sum of votes, and inclusion of founding member votes. Compared with IMF and World Bank, AIIB has taken a big step to increase the proportion of basic votes in the aggregate sum of votes, which denotes a gesture to be more progressive in pursuing a relatively fair representation from the fundamental level. However, the proportion of basic votes in the aggregate sum of votes, namely 12%, marks a retrogressive move compared with 20% of ADB. As a countermeasure, the Bank has put forward a change in the composition of the voting power by including founding member votes.

This change-through-continuity voting arrangement could be analyzed from different angles: firstly, since AIIB still positions itself as a regional MDB, it's of importance to draw reference from its regional counterpart, ADB, to bring in the relatively sound arrangements, and also displays its novel, progressive and innovative aspects in comparison with the traditional Bretton Woods institutions. Secondly, the inclusion of founding member votes is a tactic to attract more prospective members to join the Bank and enlarge its clout, especially in the preparatory stage of the Bank.

As mentioned above, it's interesting to further investigate how the shares of capital subscriptions and voting powers are played out in the Bank itself. The Schedule A in the Banks' AOA has clearly presented the initial subscriptions to the authorized capital stock, from which we could examine different members' capital subscription and voting powers. China has the dominant share of capital subscription at 32.3796%, along with a larger voting power at 27.8450%, followed by India (9.0976% capital subscription, 8.0294% voting power), Russia (7.1067% capital subscription, 6.3349% voting power), Germany (4.8756% capital subscription, 4.4360% voting power), South Korea (4.0650% capital subscription, 3.7461% voting power) and Australia (4.0134% capital subscription, 3.7021% voting power).<sup>108</sup>

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<sup>108</sup> Asian Infrastructure Investment Bank(AIIB), 2017. AIIB, Members and Prospective Members of the Bank. [online] Available at: <<https://www.aiib.org/en/about-aiib/governance/members-of-bank/index.html>> [Accessed 20 January 2017].

Astonishingly, China's voting power has been largely improved in AIIB, compared with that in the Fund(6.09%), World Bank( 4.56%), and ADB (5.454%).<sup>109</sup> This particular design outcome was partially contributed to by China's strong advocacy of improving global economic governance to increase the representation and voice of emerging markets and developing countries.<sup>110</sup> And meanwhile, it is also a matter of fact that other economically influential countries such as the U.S. and Japan haven't joined the Bank as founding members. Deliberately or naturally, this current allocation of voting powers has produced a phenomenal outcome, as stated in the 2nd clause of Article 28, decisions involving organizational structure, membership, change of authorized capital, and other significant issues require a super majority vote, which shall represent not less than three-fourths of the total voting power of the members,<sup>111</sup> thereby giving China a *de facto* veto.

The Bank's president, Jin Liqun, has elaborated upon the actual outcome of China's acquisition of veto power, owing it to China's economic weight within member countries, and further expressing that China does not deliberately pursue or will not exercise its veto right over the Bank, and with the enlargement of the membership, China's voting power will be gradually reduced and therefore the *de facto* veto power will not be retained.<sup>112</sup> Jin's clarification of China's *de facto* veto power within AIIB is not without a base for it. As mentioned above, a fixed super majority vote has been introduced into the crucial decision-making process, comprising a fixed two-thirds of the number of members and representing a fixed three-quarters of the voting power, which is identical to World Bank and ADB. China's *de facto* veto power will be largely restrained, due to the cost of exercising it, destroying the credibility and mutual trust accumulated from the preparatory stage,

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<sup>109</sup> See Asian Development Bank, 2016. *50 Years of ADB: Improving Lives for A Better Future* 2016 Annual Report. [online] Available at: <<https://www.adb.org/sites/default/files/institutional-document/237881/adb-annual-report-2016.pdf>> [Accessed 25 April 2017].

International Bank for Reconstruction and Development, 2017. *International Bank for Reconstruction and Development Subscriptions and Voting power of Members Countries*. [pdf] IBRD. Available at: <<http://siteresources.worldbank.org/BODINT/Resources/278027-1215524804501/IBRDCountryVotingTable.pdf>> [Accessed 09 March 2017].

International Monetary Fund (IMF), 2017. IMF Members' Quotas and Voting Power, and IMF Board of Governors. [online] Available at: <<http://www.imf.org/external/np/sec/memdir/members.asp>> [Accessed 22 March 2017].

<sup>110</sup> MFA, 2016. *Keynote Speech by H.E. Xi Jinping, President of the People's Republic of China, at the Opening Ceremony of the B20 Summit*. [online] Available at:

<[http://www.fmprc.gov.cn/mfa\\_eng/wjdt\\_665385/zyjh\\_665391/t1396112.shtml](http://www.fmprc.gov.cn/mfa_eng/wjdt_665385/zyjh_665391/t1396112.shtml)> [Accessed 16 March 2017].

<sup>111</sup> AIIB, AOA, Article 28.

<sup>112</sup> Fu, J., 2016. AIIB chief rules out China veto power, China Daily, [online] 27 January 2016. Available at: <[http://www.chinadaily.com.cn/business/2016-01/27/content\\_23265846.htm](http://www.chinadaily.com.cn/business/2016-01/27/content_23265846.htm)> [Accessed 15 April 2017].

outside perceptions about China and the Bank's long-term operation and survival. In addition, there is a possible scenario in which the Bank's inclusion of the U.S. and Japan will likely change the allocation of subscribed capital and voting shares, possibly diluting China's voting power to 20.5% without retaining veto power, and therefore better balancing the representation and authority structure of the Bank.<sup>113</sup> In this regard, China's individual control and overall asymmetry of control within the Bank will be largely reduced and rebalanced.

## **4.2 'China's Status: A Revisionist Reformist' in AIIB's Institutional Design**

As a foreword, it is not arguable and compelling to simply assert that AIIB is another made-in-China product, based in China and inundated with Chinese techniques, values and norms. Rather, it is to say that China has played an irreplaceable role in underpinning the institutional design of the AIIB and its policy, thus China's role should not be underestimated. In the light of China's multi-functional roles in the Bank, it is of significance to probe into the connectivity between China's status as a revisionist reformist and the Bank's institutional design, to explore in what way the Bank's institutional design acts as a channel for China to articulate its values, norms and agendas.

### **4.2.1 Non-conditionality and International Character**

China's status being a revisionist reformist has been largely reflected by its emphasis on non-conditionality and international character of the Bank. The purposes and functions of the Bank are set out in a very specific, exhaustive and transparent manner, making no mention of political goals, but instead highlighting the Bank's international character in Article 31; to refrain from all attempts that may potentially prejudice, limit, deflect or alter the Bank's purpose and functions, and only economic considerations shall be relevant to the Bank's decisions.<sup>114</sup> This special mention of the international character of the Bank, featured by non-political strings attached and full respect to the originally economic purpose, also exhibits itself as a change-through-continuity feature extended on non-conditionality, at least as manifest in the form of the original founding documents.

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<sup>113</sup> Kawai, M., 2015, p.15.

<sup>114</sup> AIIB, AOA, Article 31.

The continuity side is reflected by its exhaustive and well-defined purposes as they are manifest in their respective founding documents, in which all of them share a common characteristic of not mentioning more ‘political aims’ such as promoting democracy and practicing rule of law, while explicitly mentioning its due attention to economy and efficiency in accordance with the purposes of the institution themselves. Article III of IBRD’s AOA clarifies one of the principles of the use of loans:

“(b) The Bank shall make arrangements to ensure that the proceeds of any loan are used only for the purposes for which the loan was granted, with due attention to considerations of economy and efficiency and without regard to political or other non-economic influences or considerations.”<sup>115</sup>

And Article 14 of the ADB Charter also states one of the operating principles:

“(xi) The Bank shall take the necessary measures to ensure that the proceeds of any loan made, guaranteed or participated in by the Bank are used only for the purposes for which the loan was granted and with due attention to considerations of economy and efficiency.”<sup>116</sup>

Though manifest in the founding documents, stringent conditionality is now and then practiced by the Fund and World Bank, such as IMF structural adjustment policies on the basis of free market neoliberal principles. The conditionality imposed by the Fund and World Bank has received many criticisms, as argued by Joseph Stiglitz; conditionality is initially designed to increase the likelihood of the loans being paid back by recipient countries, but has incorporated more forceful conditions, therefore turning loans into a policy tool that further goes beyond economic sector into areas which properly belong in the realm of politics.<sup>117</sup> China is opposed to conditionality and is deeply concerned with political threats towards China’s long-term interests either nationally or globally, adamantly espousing a view that borrower nations’ sovereign rights should not be treated as a bargaining chip for doing business with the Fund and World Bank.<sup>118</sup>

Considering this, the change side is exhibited by the Bank’s more comprehensive and exhaustive listing of requirements for upholding the Bank’s international character, facilitated by extending the relevant principles from the use of loans to the staff of the Bank, and establishing a two-way process of both ruling out any political

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<sup>115</sup> IBRD, AOA, Article III Section 5(b).

<sup>116</sup> ADB, Charter, Article 14.

<sup>117</sup> Stiglitz, J. E., 2002. *Globalization and Its Discontents*. London: Allen Lane/Penguin books. pp.44-45.

<sup>118</sup> Chow, D., 2016. pp.1279-1281.

or non-economic interference in any member and refraining from any unnecessary force in influencing decision-making of the staff, who are expected to owe their duty completely to the Bank instead of any other authority.

While in retrospect, China's emphasis on non-conditionality has been long rooted, dating back to the foundation of People's Republic of China (PRC). In the 1960s, "eight principles of foreign aid" had been put forward by then Chinese Premier Zhou Enlai, to further elaborate the principle, purpose and impact of China's foreign aid programs to African countries and better govern China's overall foreign economic and technical assistance. The first two principles clearly state China's stance in providing aid to other countries is based on the 'principle of equality and mutual benefit', China never acknowledges its assistance as unilateral charity but rather mutual aid, and meanwhile China 'never attaches any conditions or asks for any privileges in its foreign aid programs'.<sup>119</sup>

Regarding Xi Jinping's leadership in China, these traditionally widely held principles have been reaffirmed and manifested in foreign aid policy, as stated by the 2014 China's Foreign Aid White Paper. Principles including non-conditionality, mutual benefits and equality are presented by its coherence and consistency.

"When providing foreign assistance, China adheres to the principles of *not imposing any political conditions, not interfering in the internal affairs* of the recipient countries and fully respecting their right to independently choosing their own paths and models of development. The basic principles China upholds in providing foreign assistance are *mutual respect, equality, keeping promise, mutual benefits and win-win*."<sup>120</sup>

When further reading the white paper, the aid programs in infrastructure construction have been highlighted as an important element for improving the recipient countries' economic development, explicitly, China has arranged a combination of grants, interest-free loans and concessional loans to assist recipient countries with essentially needed infrastructure construction.<sup>121</sup> By this token, the AIIB could be seen as a good spot and trial to strategically combine infrastructure construction and the non-conditionality principle with mutual benefits. With the

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<sup>119</sup> State Council, 1964. *State Council PRC Gazette Issue No. 2 Serial No.290*. [online] Available at: <<http://www.gov.cn/gongbao/shuju/1964/gwyb196402.pdf>> [Accessed 18 March 2017].

<sup>120</sup> State Council, 2014. *China's Foreign Aid (2014)*. [online] Available at: <[http://english.gov.cn/archive/white\\_paper/2014/08/23/content\\_281474982986592.htm](http://english.gov.cn/archive/white_paper/2014/08/23/content_281474982986592.htm)> [Accessed 28 March 2017].

<sup>121</sup> Ibid.

acknowledgement of the background knowledge, it is arguable that the principle of non-conditionality is strongly embodied in the Bank's institutional design and policy framework.

#### **4.2.2 “Democratizing” the Global Economic Governance**

As mentioned above, China has been proactively advocating for reformation of the existing global economic governance. More specifically, with global financial governance, the Bretton Woods institutions and ADB, which are largely dominated by G7 countries, take a reluctant stance to make necessary and adaptive adjustments to reflect the changing realities (the growing economic clout of the emerging economies) and better accommodate the expanded economic power, along with an increased representation and voice in the existing global economic framework.

With respect to China, its continuously increasing economic clout marks a stark contrast with the gap between its according financial power and voting power in the Fund, World Bank and ADB. As argued, this fact largely contributes to an increasing legitimacy deficit, which is further aggravated by controversial reactions to regional and global financial crises in the existing financial institutions. In light of this reality, the Board of Governors of the Fund has officially approved the 2010 Quota and Governance Reforms, which would generate a new realignment in the ranking of quota shares, allow a shift of more than 6 percent of quota shares to the dynamic emerging market and developing countries, and four emerging market countries (namely the BRICs countries) would be among the ten largest members of the Fund.<sup>122</sup> In spite of the modesty of the proposed adjustment, the U.S. Congress had repeatedly failed to sanction the IMF governance reform until congressional approval in December 2015, partly due to the concerns that the deal would relatively weaken U.S. influence in the Fund, despite the U.S retaining the veto power with the reform authorized.

Despite the incremental voting shares taking place in a slow-paced manner, China's role in both Bretton Woods institutions and ADB still remain under-valued in comparison with the dominant roles played by U.S. and Japan. It's of logic and reason

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<sup>122</sup> International Monetary Fund(IMF), 2015. IMF Managing Director Christine Lagarde Welcomes U.S. Congressional Approval of the 2010 Quota and Governance Reforms [press release] 18 December 2015. Available at: <<http://www.imf.org/external/np/sec/pr/2015/pr15573.htm>> [Accessed 22 March 2017].

to argue that China seems to have reached a conclusion that any kind of reform of the existing institutions for improving the representation and voice for emerging economic powers would be rather difficult, due to the unwillingness, intransigence and vested interests from the U.S. and Japan.<sup>123</sup>

Partly motivated and justified by pursuing more representation and voice for emerging markets and developing countries, it is therefore of importance to critically verify this pursuit by examining how China's being a revisionist reformist is manifested in the institutional design of the Bank, by way of elevating voting shares for emerging markets and developing countries. There are two comparisons conducted to see the increased voting power of same member countries (limited to emerging market and developing economies<sup>124</sup>) in the Bank, the Fund, IBRD and ADB.

*Comparison 1 : Increased Voting Power (AIIB in comparison with the Fund, and IBRD)*

As presented by Figure 4, the increased voting power is calculated by measuring the differences between the voting power of member countries in AIIB and voting power in the IMF and IBRD respectively. Self-evidently, most of the increased voting power rates are positive, except that Saudi Arabia's relative voting power in IBRD is larger than that in AIIB. The vast majority of the same emerging and developing economies have witnessed an increasing trend in terms of their voting power in the Bank, which is generally in line with China's appeal for increasing the representation and voice of emerging markets and developing countries. A further investigation of the distribution of the increased voting power, it presents a noteworthy feature that some major developing economies, such as China, India, Russia and Indonesia, take the lead, while the rest of the developing economies' increased voting power is rather minimum or limited. Thus, it denotes the fact that this new Bank is inclined to give more representation and voice to those major developing countries, rather than the

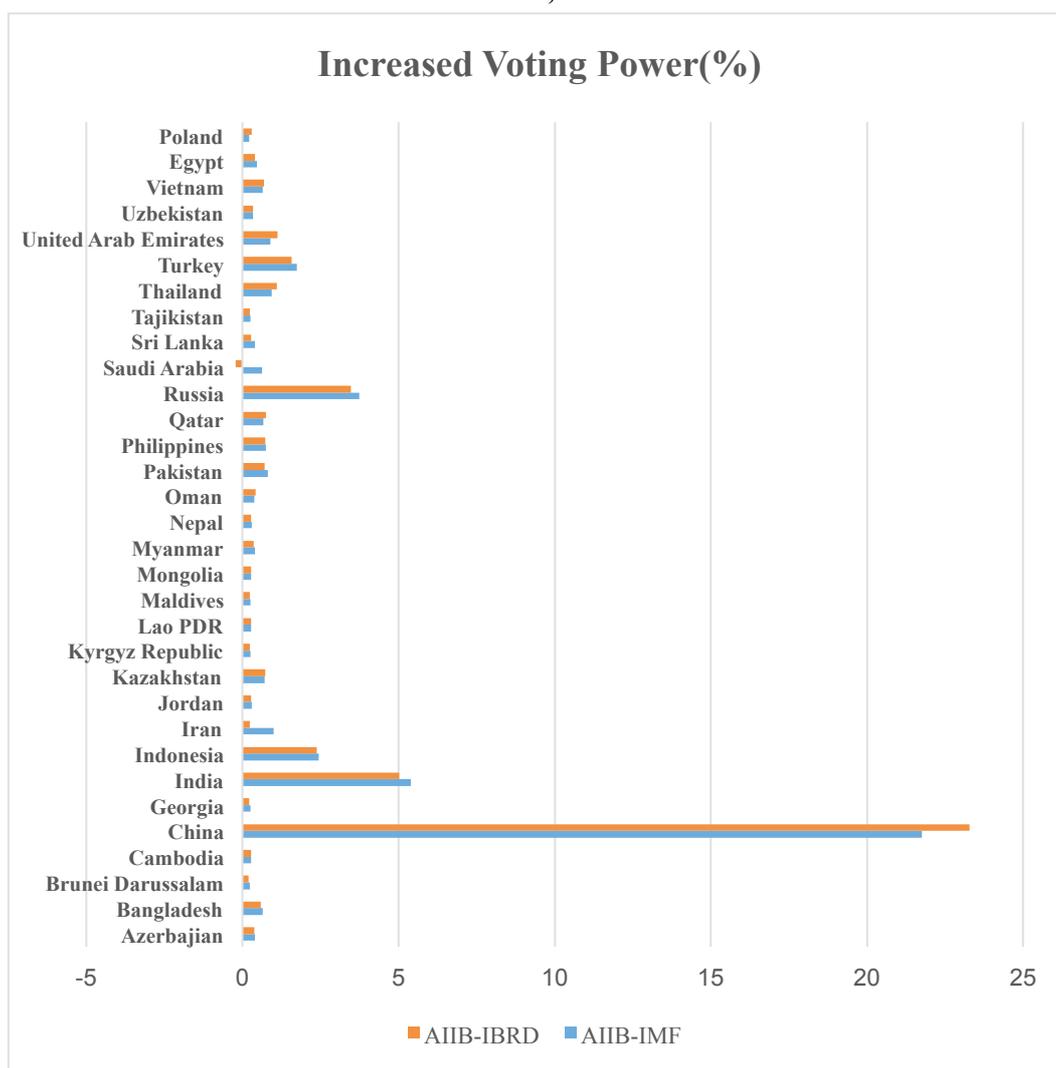
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<sup>123</sup> Kawai, M., 2015. p.12.

<sup>124</sup> The emerging market and developing economies is based on the classification of countries adopted by World Economic Outlook (WEO), a survey by the IMF staff published twice a year in the spring and fall. See World Economic Outlook, April 2017: Gaining Momentum? World Economic Outlook (WEO), 2017. *World Economic Outlook, April 2017: Gaining Momentum?* [pdf] IMF. Available at: <<http://www.imf.org/en/Publications/WEO/Issues/2017/04/04/world-economic-outlook-april-2017#>> [Accessed 25 March 2017].

vast majority of developing countries, since their increased voting power is largely contributed to by the Bank's current small membership size, which provides an opportunity to share the fixed pool of voting power with less competing countries. In this regard, with the increasing enlargement of membership in the Bank, the dynamics of the voting powers acquired by the vast majority of developing countries is worth being delved into and compared with IMF and IBRD.

**Figure 4. Increased Voting power of the Same Emerging and Developing Economies in AIIB, IMF and IBRD**



Source: AIIB, IMF and IBRD.

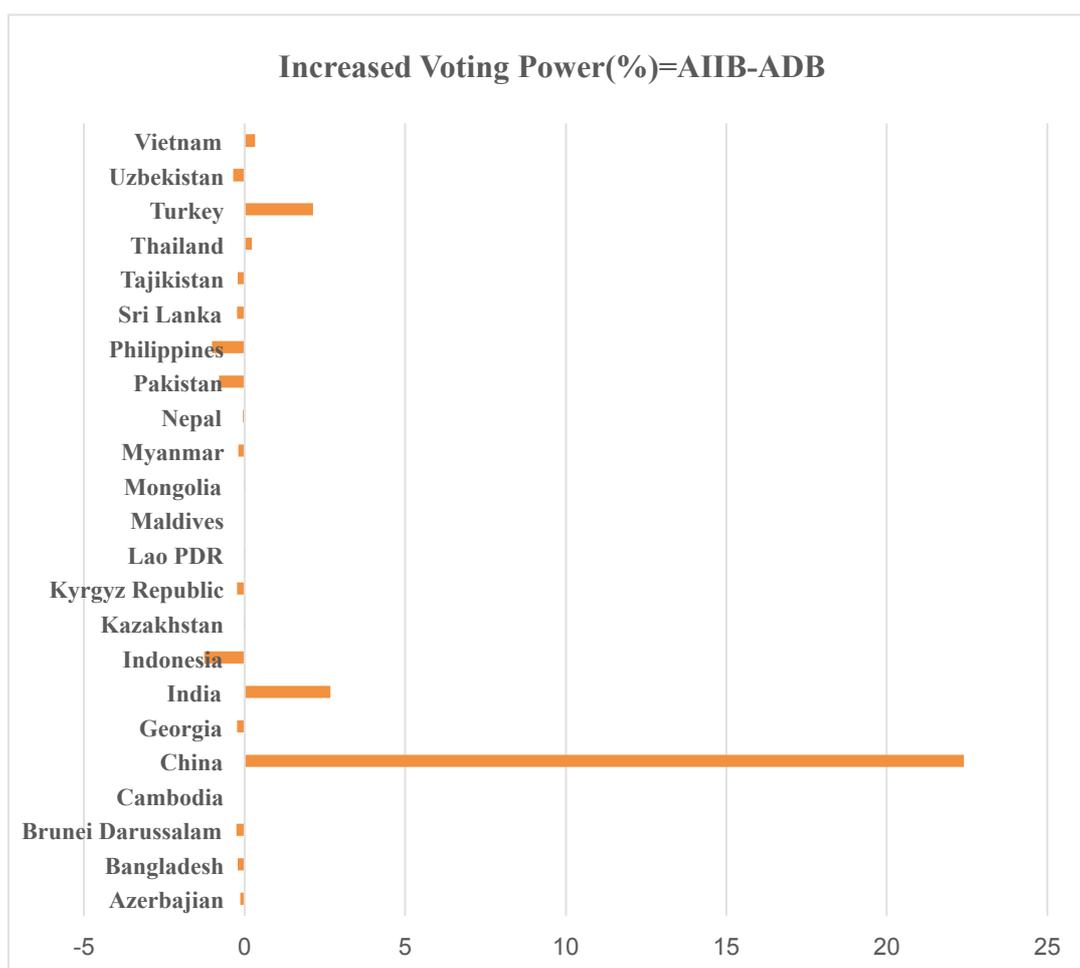
*Comparison 2 : Increased Voting Power (AIIB in comparison with ADB)*

The findings as mentioned above, are further testified by Figure 5, which presents increased voting power by calculating the difference between the voting power of

member countries in AIIB and that in ADB. Generally, the increased voting powers of China, India, Turkey, Vietnam, and Thailand are positive, while the rest of the majority's increased voting powers approach zero and negative figures. Arguably, as ADB's regional counterpart, the voting power in AIIB is more tailored to increasing the representation and voice of some major developing economies rather than the vast majority of developing countries.

This finding does not intend to simply suggest any one-sided or arbitrary assessment of the overall quality of the Bank, conversely, it is to denote that the Bank's allocation of the voting powers does give us a transparent, comparable and verifiable indication that the Bank hasn't presented a novel practice of restructuring the financial architecture. It is fair to say, instead it takes on a feature of creating a new frame that largely subscribes to the rules of the existing game in town.

**Figure 5. Increased Voting power of the Same Emerging and Developing Economies in AIIB and ADB**



Source: AIIB and ADB.

### 4.3 Bounded Rationality: Inside and Beyond the Institutional Design of AIIB

In light of aforementioned analysis, it is of significance to provide a self-reflexive revisit of the rational institutional design of the Bank. As critically discussed, the institutional design of AIIB has largely demonstrated a feature of change-through-continuity, incorporating a certain spectrum of institutional isomorphism, all the while displaying a certain degree of modification or variation. This change-through-continuity characteristic is not to say that the Bank's institutional design is wholly novel and innovative. It doesn't strictly conform to comprehensive rationality, which assumes that preferences are defined over the known and fixed outcomes where the decision maker will resort to the optimization of their net benefits, or subjective expected-utilities in the manner of resorting to choosing the alternative that yields the highest level of benefits.<sup>125</sup> Instead, it is to say that the Bank's institutional design is manifested in a fashion more geared towards the bounded rationality as proposed by Herbert Simon, which assumes that decision-makers are goal-oriented and adaptive with intended rationality, but occasionally fail to accomplish certain goals due to interactions between aspects of their cognitive architectures and the underlying structures of the environment faced by them.<sup>126</sup>

In this sense, under the rational design framework, bounded rationality provides an additional insight for us to critically explain why change-through-continuity is manifested in the institutional design of the Bank. As for the membership, the Bank has potentially opened its arms to embrace more prospective members that are not strictly restricted to sovereign countries. However, Taiwan is a witness to the Bank's institutional design in the form of bounded rationality, further revealing that joining the Bank is simply a matter of economic accounts, and rather squinted towards an interplay of economy and politics mingled with power and discourse.

Further, the issue scope has been initially restricted to infrastructure investment, which could also be seen as a showcase of China's bounded rationality in utilizing its comparative advantage drawn from the past development, to advance its strategic agendas in a multilateral setting under the official framework of mutual benefits.

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<sup>125</sup> Jones, B. D., 1991. Bounded Rationality, *Annual Review of Political Science*. *Annual Review of Political Science*, 2(1), p.299.

<sup>126</sup> Jones, B. D., 2003. Bounded Rationality and Political Science: Lessons from Public Administration and Public Policy. *Journal of Public Administration Research and Theory*, 13(4), p.397.

China's cognitive conditions indicate a considerable part of the impetus for carefully selecting infrastructure investment as the entry point for running the Bank.

Another angle to investigate the bounded rationality of designing the Bank goes to the gap between China's normative appeals and the outcome of the practice. China's normative appeals are manifested in its advocacy of non-conditionality, mutual benefits and equality. However, it is worthy to note that the Chinese concept of equality seems to be contingent upon specific circumstances. Without any doubt, in political and cultural realms, China has been conforming to the principle of sovereign equality and non-intervention as a means to preserve uniqueness and diversity. While in the economic realm, as presented by Xi Jinping's speeches, China has repeatedly called for improving global economic governance on the basis of equality, a concept that embodies reflecting new realities of the world economic landscape, increasing representation and voice of emerging markets and developing economies, and ensuring all countries have equal rights, opportunities and rules to follow in international economic cooperation.<sup>127</sup>

It indeed partially reflects the equality agenda in the Bank's institutional design when seeing the increased voting shares by the developing countries compared with those in the Bretton Woods institutions, while it also demonstrates a certain degree of retrogression in comparison with ADB in terms of protecting the voting powers of the developing countries with minor economic importance. Objectively, this small retrogression is not to say a fault of inconsistency or self-contradiction due to China's failure in fulfilling the normative appeals, but rather, it is overwhelmingly contributed to by the underlying structures in the existing international financial architecture, displaying a co-constitution of the economic power and invested interests. The change-through-continuity characteristic fundamentally reveals that a novel re-structuring of the existing international financial architecture is too complex to achieve in a short time-span, compared with a pragmatic manner of 'bringing forth the new through the old' in the practice of bounded rationality.

In addition, the bounded rationality, reflected by the change-through-continuity feature of the Bank's institutional design, also helps us to shed light upon how to better understand the connectivity between the ideational appeals and practical

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<sup>127</sup> MFA, 2016. Keynote Speech by H.E. Xi Jinping, President of the People's Republic of China, at the Opening Ceremony of the B20 Summit.

outcomes of proposed political or economic initiatives. The key is to combine the insights derived from both the systematic understanding of the original internal context and the underlying structures and complexities in the external background where the economic and political agendas have to reach out.

## CHAPTER 5 CONCLUSION AND OUTLOOK

### *Conclusion*

This thesis has addressed the two main research questions, ‘what characteristic does the Bank possess regarding institutional design, in comparison with the Fund, World Bank and ADB?’ and ‘what role has China played in contributing to the characteristic of the Bank’s institutional design?’. In order to answer these two questions, using the rational institutional design as the theoretical framework has allowed for a more systematic and in-depth discussion of different aspects of the Bank’s institutional design and China’s corresponding roles in it.

Overall, this thesis has found out that change-through-continuity is a recurring characteristic of the institutional design of the Bank, in comparison with the IMF, World Bank and ADB. More concretely, with respect to membership, the Bank has extended its membership from strictly-defined ‘sovereign countries’ to a more inclusive stance, opening the membership door for applicants like a territory entity that is not sovereign or does not hold responsibility for its conducts of international relations. With respect to scope issue, the Bank has also focused on promoting sustainable economic and social development through cooperation, but has initially confined its scope issue to infrastructure investment. With regards to centralization, albeit following the typical three-layered organizational structure commonly adopted by the Fund, World Bank and ADB, the Bank has adopted a non-resident board, which reflects a process of co-constitution of centralization and de-centralization, but is more prone to centralization. Concerning voting, the Bank has followed the commonly used weighted voting system in the Bretton Woods institutions and ADB, but also adds one category of founding member votes as one constituent of the voting shares.

China, as a revisionist reformist, has played a significant role in shaping the Bank’s institutional design, embodying its emphasis on non-conditionality and international character in line with the change-through-continuity feature of the institutional design, and advocating for reforming global economic governance. To sum up, the change-through-continuity feature of the Bank’s institutional design largely reflects bounded rationality, which is added as a self-reflexive thought for better reflecting upon why especially change and continuity are reflected in the

Bank's institutional design.

*Outlook*

As aforementioned, there are some follow-up questions to be raised. How does this change-through-continuity characteristic of the Bank's institutional design influence the Bank's operation and future development? Will this feature be weakened or strengthened when the U.S. and Japan possibly join the Bank? These intriguing questions are of enough value and importance to warrant in-depth future research.

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