
Aims and Prospects of the Asian Infrastructure Investment Bank Proposed by China

Eiichi Sekine

*Chief Representative, Beijing Representative Office
Nomura Institute of Capital Markets Research*

I. Asian Infrastructure Investment Bank launched as new multilateral development bank

A Memorandum of Understanding (MoU) regarding the founding of the Asian Infrastructure Investment Bank (AIIB) proposed by the Chinese government was signed by the founding member nations in Beijing on 24 October 2014, ahead of the Asia Pacific Economic Cooperation (APEC) summit that was also held in the Chinese capital on 10–11 November. The MoU was signed by 21 nations, mostly Asian countries. The signing ceremony was attended by Chinese President Xi Jinping, who thanked and congratulated the signing founding members on the occasion.

The AIIB concept was first proposed by Chinese President Xi Jinping and Prime Minister Li Keqiang during their respective October 2013 tours of Southeast Asian nations as a new China-led multilateral development bank (MDB) and part of the new Silk Road Development initiative¹. The proposal has since attracted the attention of governments and market participants around the world. On five occasions from January to September 2014, multilateral talks were held with representatives of nations in favor of the AIIB's foundation, with the China delegation headed by Jin Liqun, formerly China's Vice Minister of Finance (equivalent to a vice minister in Japan), Vice-President of the Asian Development Bank (ADB), and Chairman of the Board of Supervisors of the sovereign wealth fund, China Investment Corporation (CIC).

The list of AIIB prospective founding members (PFMs) underwent major changes prior to the application deadline on 31 March 2015. On 12 March 2015, the United Kingdom became the first G7 nation to announce it would be a founding member. It was followed by Germany, France, and Italy on 17 March. Thereafter, one country after another applied for acceptance as founding members, and after a two-week review period by the original PFMs the final group of 57 founding members was announced on 15 April (Figure 1). As a number of these founding members are also contributors to the ADB, role-sharing among the existing MDBs and the new AIIB is a topic of keen interest.

¹ Also called the Silk Road Economic Belt initiative.

Figure 1: AIIB founding members

No.	Region	Founding member nation (region)	Application date	Approval date
1	East Asia	China	MoU signatory	24 October 2014
2		Mongolia	MoU signatory	24 October 2014
3		South Korea	27 March 2015	11 April 2015
4	Southeast Asia	Singapore	MoU signatory	24 October 2014
5		Thailand	MoU signatory	24 October 2014
6		Malaysia	MoU signatory	24 October 2014
7		Brunei	MoU signatory	24 October 2014
8		Philippines	MoU signatory	24 October 2014
9		Cambodia	MoU signatory	24 October 2014
10		Laos	MoU signatory	24 October 2014
11		Myanmar	MoU signatory	24 October 2014
12		Vietnam	MoU signatory	24 October 2014
13		Indonesia	-	25 November 2014
14	Oceania	New Zealand	-	01 January 2015
15		Australia	29 March 2015	13 April 2015
16	South Asia	India	MoU signatory	24 October 2014
17		Nepal	MoU signatory	24 October 2014
18		Bangladesh	MoU signatory	24 October 2014
19		Sri Lanka	MoU signatory	24 October 2014
20		Pakistan	MoU signatory	24 October 2014
21		Maldives	-	31 December 2014
22	Former Soviet Union, Central Asia	Kazakhstan	MoU signatory	24 October 2014
23		Uzbekistan	MoU signatory	24 October 2014
24		Tajikistan	-	13 January 2015
25		Georgia	28 March 2015	12 April 2015
26		Russia	30 March 2015	14 April 2015
27		Kyrgyzstan	31 March 2015	09 April 2015
28	Azerbaijan	-	15 April 2015	
29	Middle East	Oman	MoU signatory	24 October 2014
30		Qatar	MoU signatory	24 October 2014
31		Kuwait	MoU signatory	24 October 2014
32		Saudi Arabia	-	13 January 2015
33		Jordan	-	07 February 2015
34		Turkey	26 March 2015	10 April 2015
35		Israel	31 March 2015 (not announced by MoF)	15 April 2015
36		Iran	-	03 April 2015
37		UAE	-	03 April 2015
38	Europe	UK	12 March 2015	28 March 2015
39		France	17 March 2015 (announced by MoF)	02 April 2015
40		Italy	17 March 2015 (announced by MoF)	02 April 2015
41		Germany	17 March 2015 (announced by MoF)	01 April 2015
42		Luxembourg	18 March 2015	27 March 2015
43		Swiss	20 March 2015	28 March 2015
44		Austria	27 March 2015	11 April 2015
45		Netherlands	28 March 2015	12 April 2015
46		Denmark	28 March 2015	12 April 2015
47		Finland	30 March 2015	12 April 2015
48		Sweden	31 March 2015	15 April 2015
49		Iceland	31 March 2015	15 April 2015
50		Portugal	31 March 2015	15 April 2015
51		Norway	31 March 2015 (not announced by MoF)	14 April 2015
52		Malta	-	09 April 2015
53		Spain	-	11 April 2015
54		Poland	-	15 April 2015
55	Latin America	Brazil	28 March 2015	12 April 2015
56	Africa	Egypt	30 March 2015	14 April 2015
57		South Africa	-	15 April 2015

Note: Shaded area shows those nations considered to be intra-regional members (as per 16 April 2015 issue of the Nihon Keizai Shimbun).

Source: Nomura Institute of Capital Markets Research, based on data from China's Ministry of Finance

II. Overview of AIIB's current structure

1. AIIB overview at time of founding members' confirmation

The establishment of the AIIB has been the responsibility of China's Ministry of Finance (MoF), with Vice Minister Shi Yaobin heading the ministry's effort. A summary version of the MoU can be found (in Chinese) on the MoF's website². After the MoU signing, a Q&A session with MoF Minister Lou Jiwei on the AIIB's establishment was posted on the ministry's website³. Based on these webpages and other public disclosures by China's MoF, we have compiled the following outline of the AIIB.

1) Founding members

The 57 founding nations include three from East Asia, 10 from Southeast Asia, two from Oceania, six from South Asia, seven from Central Asia and former states of the Soviet Union, nine from the Middle East, 17 from Europe, one from Latin America, and two from Africa (Figure 1). China's MoF has announced that 37 members are from Asia while the other 20 are from other regions (although the MoF has not provided a specific list of countries in this broad categorization).

2) Positioning, scale and headquarters

The AIIB is positioned as an intergovernmental mechanism for supporting multilateral development in Asia with an emphasis on infrastructure construction.

Drawing on the model and management examples of existing MDBs, the AIIB plans to cooperate closely with multilateral and bilateral development finance institutions, such as the World Bank and the ADB, and to promote regional cooperation and partnerships in order to jointly address the infrastructure needs of the Asian region.

The Bank is to be capitalized at \$50 billion initially, with ultimate authorized capital of \$100 billion. It will be headquartered in Beijing.

3) Road to establishment

Following the signing of the founding MoU, the first step in the AIIB's road to establishment is the negotiations on the Articles of Agreement among all nations interested in joining the Bank. The nations that signed the establishment agreement become the AIIB's Founding Members, but the Chinese government is welcoming other interested nations to the negotiating table under "the principle of open and inclusive regionalism."

² http://gjs.mof.gov.cn/pindaoliebiao/gongzuodongtai/201410/t20141030_1155021.html (in Chinese)

³ http://www.mof.gov.cn/zhengwuxinxi/caizhengxinwen/201410/t20141027_1154454.html (in Chinese)

After the negotiations on the Articles of Agreement conclude in June 2015, the plan is for the AIIB to begin operations by the end of the year. Just a bit more than one month after the MoU signing, on 28 November 2014, the chief negotiators from the original group of founding members (MoU signatories) met in Kunming City in China's Yunnan Province for the first round of negotiations on the Articles of Agreement. The second round was held on 15–16 January in Mumbai, India, followed by the third round on 30–31 January in Astana, Kazakhstan, and the fourth round on 27–28 April in Beijing. The final fifth round was on 20–22 May in Singapore.

2. Questions raised by other countries about AIIB's establishment

A number of other countries have raised various questions about the AIIB's establishment. Most notably, the United States and Japan, the two largest funders of the ADB (Figure 2), are thought to have some serious concerns about the AIIB.

Figure 2: Equity ratios of ADB capital providing nations (end-December 2013)

Non-borrowing nations	Equity ratios	Borrowing nations	Equity ratios
Japan	15.7%	China	6.5%
US	15.6%	India	6.4%
Australia	5.8%	Indonesia	5.2%
Canada	5.3%	Malaysia	2.7%
South Korea	5.1%	Philippines	2.4%
Germany	4.3%	Pakistan	2.2%
France	2.3%	Thailand	1.4%
UK	2.1%	Bangladesh	1.0%
Italy	1.8%	Other	5.4%
Other	9.0%		
27 countries	66.9%	40 countries	33.1%

Source: Nomura Institute of Capital Markets Research, based on ADB data

1) U.S. concerns

For example, U.S. Secretary of State John Kerry welcomed the idea of an infrastructure-financing bank in Asia, but told China that the bank needs to meet international standards for governance and transparency (China Daily, 25 October 2014)⁴. Secretary Kerry personally asked Australian Prime Minister Tony Abbot to refrain from joining the AIIB (same issue of China Daily), and the two announced that their countries would not join the AIIB at their joint press conference on 31 October 2014⁵. Australia had originally indicated a positive stance on signing the MoU on AIIB establishment⁶.

⁴ http://usa.chinadaily.com.cn/world/2014-10/25/content_18800563.htm

⁵ Nihon Keizai Shimbun, 1 November 2014 morning edition (in Japanese)

⁶ Nihon Keizai Shimbun, 21 October 2014 morning edition (in Japanese)

South Korea and Indonesia were two other countries whose movements were being watched closely, but neither was present at the MoU signing on 24 October 2014. Thereafter, however, all three decided to become founding members, as shown in Figure 1.

2) Japan's concerns

The Japanese government also questioned the AIIB's governance and transparency.

At a press conference on 2 September 2014, Foreign Minister Fumio Kishida indicated that Japan would have to give careful consideration to participation in the AIIB. Specifically, he mentioned three points: (1) whether a new international institution in addition to the existing MDBs, such as the ADB, would provide added value, (2) whether an institution in which one country has an extremely large equity ratio can achieve fair governance worthy of being called an international institution, and (3) whether the proposed institution will ensure that it does not damage other creditors by providing lending that disregards debt sustainability⁷.

Also, at a press conference on 24 October 2014, Finance Minister Taro Aso commented that, while the AIIB in and of itself was not a bad idea, he was concerned about its audit capabilities and the relation between China's large equity ratio and transparency of the bank's management.⁸ Finally, materials presented at the 24th Meeting of the Subcouncil on Foreign Exchange and Other Transactions, held by the Ministry of Finance's Council on Customs, Tariff, Foreign Exchange and Other Transactions on 7 April 2015, summarized the Japanese government's three concerns about the AIIB: (1) whether it will ensure fair governance (especially, the importance of the governing council that represents member countries auditing and approving each project), (2) whether it can ensure that it does not damage other creditors by providing lending that disregards debt sustainability, and (3) whether it will take into consideration the environmental and social impact of the projects it finances⁹.

3. Chinese government's explanations

During a Q&A session, China Finance Minister Lou Jiwei addressed the concerns raised by the United States and Japan as follows:

1) Relationship with existing MDBs

First, the AIIB is intended as a compliment to existing MDBs and will not be competing with them. The main role of MDBs such as the World Bank and the ADB is to reduce poverty around the globe. Looking at historical precedents, the establishment of

⁷ http://www.mofa.go.jp/mofaj/press/kaiken/kaiken4_000113.html (in Japanese)
http://www.mofa.go.jp/press/kaiken/kaiken4e_000097.html#topic2 (in English)

⁸ http://www.mof.go.jp/public_relations/conference/my20141024.htm (in Japanese)

⁹ https://www.mof.go.jp/about_mof/councils/customs_foreign_exchange/sub-foreign_exchange/proceedings/material/gai20150407/03.pdf (in Japanese)

the ADB and the European Bank for Reconstruction and Development (EBRD) did not weaken the impact of existing MDBs but rather enhanced the overall capacity of the world's MDBs and contributed to further development of the global economy.

Second, the AIIB intends to strengthen cooperation with existing MDBs through co-financings and similar joint efforts. Also, as an important shareholder of both the World Bank and the ADB, China will continue to actively contribute to the promotion of poverty reduction throughout the efforts of these existing MDBs.

2) Equity ratio

For starters, the nations interested in joining the AIIB agreed to base equity contributions on each nation's domestic GDP. Consequently, China became the largest capital contributor.

Secondly, China initially announced its willingness to contribute up to 50% of the AIIB's capital to show its strong support for the bank's establishment, not because it desired to be the single, largest capital contributor. China's equity share could end up below 50%. In particular, if more countries join the AIIB, China's equity ratio should accordingly.

3) Governance

Firstly, the AIIB will have a three-tiered governance structure, consisting of the Board of Governors, the Board of Directors and the Bank's management. The Board of Governors is the Bank's highest decision-making body and, according to the Articles of Agreement, can delegate authority to the Board of Directors and management.

Secondly, in its initial stages the AIIB will have a non-permanent Board of Directors that will meet each year to determine important policies and matters.

Thirdly, the AIIB will establish a supervisory audit system, with management responsible for daily operations.

Fourthly, the selection of the Bank's Secretary General and senior executives will be a public and highly transparent procedure.

4) Operations

For starters, the AIIB has great respect for and therefore will adopt many of the standards and methods of existing MDBs. It will also establish provisions to ensure financed projects are feasible and place a high priority on societal considerations (i.e., establish a system of guarantees for residents forced by their governments to resettle involuntarily). Established MDBs, such as the World Bank and ADB, have accumulated extensive experience and a wealth of best practices in key operational areas, such as governance, environmental policies, guarantee provisions related to societal

considerations, equipment procurement (for projects), fiscal evaluations of borrowing nations, and infrastructure project management.

However, the AIIB also intends to make adjustments to some of the regulations of the established MDBs in order to raise operating efficiency and improve upon current practices that are overly complicated and not highly relevant to the actual conditions.

4. Projected developments as of founding agreement negotiations stage

Negotiations on the AIIB's founding agreement, the Articles of Agreement have just begun. Based on other nations' concerns and China's explanations, we expect the following developments in coming months.

1) AIIB governance design and role-sharing

First, regarding the AIIB's governance design (organization and operation) and role-sharing, we expect AIIB officials to begin full-fledged consultations with existing MDBs.

At a press conference in Beijing on 8 July 2014, World Bank President Jim Yong Kim said he welcomed the plan to establish the AIIB¹⁰. On 23 October of the same year, ADB President Takehiko Nakao indicated his understanding of the need for the AIIB but also stressed the importance of role-sharing with the ADB during a press conference while visiting Beijing¹¹. China's Ministry of Finance, which is responsible for coordinating the establishment of the AIIB, is a conduit for applications for loans from the World Bank and the ADB. Given its relation to the two MDBs, we expect it to consult closely with both as it moves forward with plans for the AIIB. Nevertheless, we expect the United States and Japan to continue raising questions about the AIIB's governance design and plans for role-sharing with existing MDBs.

2) Adjustments to China's equity ratio and increase in countries participating in negotiations

Second, we expect China's share of capital contributions to the AIIB to undergo some adjustment. During the previously mentioned Q&A session, China Finance Minister Lou Jiwei noted that the negotiations on the Articles of Agreement for establishing the AIIB would be open to all interested nations, and not just the MoU signatories. Any resulting increase in the number of founding member nations would likely further lower China's equity ratio. In addition, China's equity ratio could undergo some adjustment depending on whether the method for determining equity ratios by GDP is based on nominal GDP values or purchasing power parity (PPP).

¹⁰ Reuters, 9 July 2014

¹¹ Nihon Keizai Shimbun, 24 October 2014 morning edition. (in Japanese)

III. AIIB from China’s perspective and key issues / AIIB and key issues from China’s perspective

Promotion of the AIIB concept is logical from the perspective of Chinese domestic politics as it fits with the new reform and opening up policy expounded by Xi Jinping’s leadership group at the Communist Party of China’s (CPC) 18th National Congress held in November 2012 and could help solve some of the issues facing the Chinese economy. Below we discuss the AIIB from China’s perspective and present the key issues.

1. Promotion of development of new Silk Road

China’s AIIB concept, as noted at the beginning of this report, has been proposed as part of Xi Jinping’s leadership group’s plan to develop a new Silk Road.

Speaking on 16 September 2014 at the 11th China–ASEAN Expo held in Guangxi Zhuang Autonomous Region in southern China along the border with Vietnam, Vice Premier Zhang Gaoli, one of the seven members of China’s top ruling group, the Politburo Standing Committee, proposed “interconnection and intercommunication” as a key area of cooperation between China and ASEAN required to realize the “21st Century Maritime Silk Road” initiative advocated by President Xi Jinping during his Southeast Asia tour in October 2013. Specifically, he proposed that China and ASEAN (1) step up efforts to build networks of maritime and river transport, high-speed roads, high-speed railways, aviation and optical cable communications, and (2) accelerate the building of the China-ASEAN Port Cities Cooperation Network and the China-ASEAN Public Information Platform for Port Logistics. Toward that end, he proposed (3) the establishment of the AIIB as an institution that will address financing bottlenecks in Southeast Asia.

The Xi Jinping leadership group’s proposal to promote development of a new Silk Road was adopted as part of the Chinese Communist Party’s reform plan at the Third Plenary Session of the 18th CPC Central Committee. Specifically, Part VII of the reform plan (“Building a New Open Economic System”) says that China “will set up development-oriented financial institutions, accelerate the construction of infrastructure connecting China with neighboring countries and regions, and work hard to build a Silk Road Economic Belt and a Maritime Silk Road, so as to form a new pattern of all-round opening”. The development of two new Silk Roads refers to creating Silk Roads traversing land and sea. In Chinese, the concept is also referred to as “One Belt and One Road”. The former of the two, the land-based Silk Road, was first proposed by President Xi Jinping during his visit to Kazakhstan in September 2013.

Development of the Silk Road will accelerate infrastructure development in China’s neighboring countries and regions, helping China secure routes needed to transport energy and food. In this sense, the Silk Road initiative is an extension of domestic politics. However, the establishment of the required infrastructure will also benefit the economies of neighboring countries and regions. Establishing a new MDB also will promote cooperation among many nations. In this sense, the Silk Road initiative can be regarded as a diplomatic initiative.

As long as Silk Road development financed by the AIIB is mainly for economic purposes, AIIB-participating nations should continue to support the idea and other concerned countries should be able to calmly watch the developments. However, if other, non-economic goals (security, etc.) become apparent, frictions between China, the participating nations, and other concerned nations will be unavoidable.

2. Leveraging foreign currency reserves and formation of a new international financial system

In addition to the AIIB, to support Silk Road development the Chinese government decided to establish a “Silk Road Fund” at the 8th meeting of Leading Group for Finance and Economics, an inner group of the Central Committee of the Chinese Communist Party, on 4 November 2014¹². Soon thereafter on 9 November, at the Dialogue on Strengthening Connectivity Partnership attended by leaders from other invited countries¹³ that are not members of the Asia Pacific Economic Cooperation (APEC) grouping, President Xi Jinping announced that China would contribute \$40 billion to the Silk Road Fund. The fund’s management company was established at the end of December 2014 (initial capital of \$10 billion), and on 20 April 2015 the management company selected its first investment project, the construction of a hydraulic power generation plant in Pakistan. The Chinese government apparently intends to use its robust foreign currency reserves, the largest in the world at about \$3.8 trillion, to fund the AIIB and the Silk Road Fund (Figure 3).

At the aforementioned party Leading Group meeting, reports were received from the National Development and Reform Commission, which is responsible for economic development, the Ministry of Finance, which deals with MDBs, and the People’s Bank of China (PBOC), which is responsible for international finance and China’s foreign reserves. In its report, the Finance Ministry indicated its intention to lead the effort to establish three new MDBs¹⁴. These three MDBs are (1) the AIIB, (2) the New Development Bank (NDB), which the BRICS nations agreed to establish as a BRICS development bank in July 2014, and (3) the Shanghai Cooperation Organization’s lending mechanism. The Shanghai Cooperation Organization (SCO) is a framework for multilateral cooperation established in 2001 by Russia, China and four central Asian nations (all former members of the Soviet Union). The SCO’s lending mechanism includes the establishment of a Shanghai Cooperation Organization Bank.

The establishment of these MDBs is likely China’s first move toward the establishment of a new international financial system. Nonetheless, at the joint press conference held by China’s President Xi and U.S. President Barack Obama following their summit meeting during the APEC summit held in Beijing in November 2014, President Xi noted that he welcomed the active participation of the United States and other relevant countries in the establishment of the AIIB and Silk Road Fund, in accordance with the two institution’s

¹² <http://cpc.people.com.cn/n/2014/1107/c64094-25990858.html> (in Chinese)

¹³ The participating non-APEC nations were Bangladesh, Tajikistan, Laos, Mongolia, Myanmar, Cambodia, and Pakistan.

¹⁴ http://gjs.mof.gov.cn/pindaoliebiao/ldjh/201404/t20140402_1062837.html (in Chinese)

principle of openness and inclusiveness¹⁵. Going forward, the China-led AIIB is likely to continue to pursue discussions and adjustments to secure cooperation and appropriate role-sharing with the existing MDBs.

Figure 3: Nations with largest foreign currency reserves

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

Note: 1. Based on foreign reserve balances of 63 nations or regions.
 2. BRICS figure is the total for Brazil, Russia, India, China and South Africa.
 Source: Nomura Institute of Capital Markets Research, from IMF data

3. Promotion of RMB internationalization

The provision of RMB-denominated loans by the AIIB for infrastructure development projects in the Asia would probably lead to expansion of the RMB offshore market and internationalization of China's currency. Vice Premier Zhang Gaoli, in his previously mentioned speech, cited the need for expanding the scale and scope of RMB currency swap agreements and expanding RMB-denominated trade settlements between China and Southeast Asian nations. He also said that a market for trading the Chinese currency and Southeast Asian currencies should be created and that cross-border cooperation was essential to the development of financial infrastructure and financial services in the region.

According to the ADB and the Asian Development Bank Institute (ADBI), Asia needs to invest about \$8 trillion in national infrastructure between 2010 and 2020¹⁶, further increasing the importance of enhancing the financial intermediation function inside and outside of Asia and promoting a shift from savings to investment. Toward that end, the AIIB will probably follow the ADB's example and supplement the capital contributions of member nations by issuing bonds in Asia and in other markets. One possibility is the issuance of RMB-denominated bonds in mainland China and the offshore market.

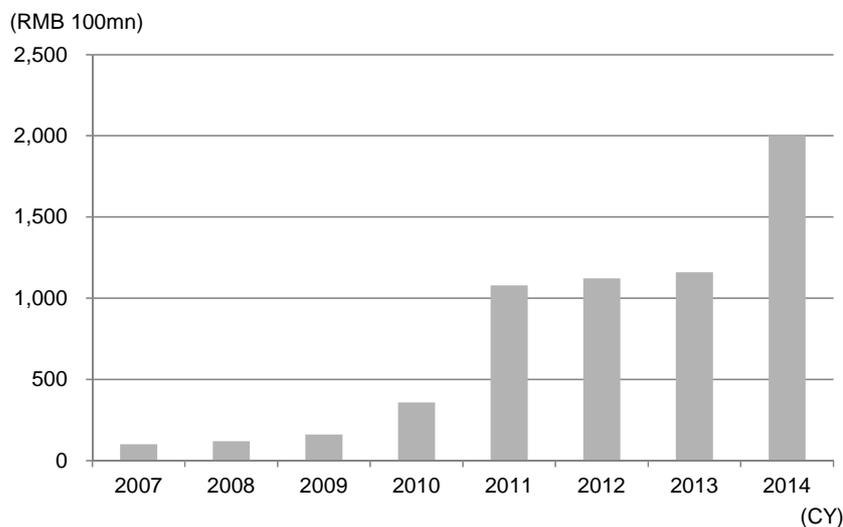
¹⁵ <http://cpc.people.com.cn/n/2014/1113/c64094-26012270.html> (in Chinese);
<https://www.whitehouse.gov/the-press-office/2014/11/12/remarks-president-obama-and-president-xi-jinping-joint-press-conference> (in English)

¹⁶ <http://www.adbi.org/book/2009/09/15/3322.infrastructure.seamless.asia/>

The issuance of RMB-denominated bonds in mainland China brings to mind the issuance of ADB's first samurai bond in 1970. Issuance of RMB-denominated bonds by MDBs would further open China's bond market to nonresident issuers. The ADB and the World Bank Group's International Finance Corporation (IFC) have issued panda bonds (RMB-denominated bonds issued in China), but the total number of issues and issuers of such bonds is still very small¹⁷. Consequently, further promotion of financial reform in China is greatly needed, as pointed out in the reform plan adopted at the Third Plenary Session of the 18th CPC Central Committee.

As for RMB-denominated bonds in offshore markets, issuance in the Hong Kong market has been expanding steadily in recent years (Figure 4). The Chinese government has issued RMB-denominated bonds in Hong Kong since 2009. In 2011, the World Bank, IFC, and ADB made their first issues of RMB-denominated bonds in Hong Kong. Whether it decides to issue bonds denominated in RMB or in other currencies, the AIIB is expected to follow in the footsteps of the existing MDBs and provide global investors with a new investment product backed by a credit rating. For example, the ADB was awarded a AAA rating by an international rating agency on the basis of its (1) solid support from investors (member countries), (2) favorable asset content and treatment of creditors, and (3) strong risk management capability supported by sound financial and risk management policies. The ADB's example indicates the importance of using existing MDBs' governance systems as a reference point.

Figure 4: Issuance of RMB-denominated bonds in Hong Kong



Note: 2014 data as announced by the Hong Kong Special Administrative Region (China Securities Journal, 26 February 2015).

Source: Nomura Institute of Capital Market Research, based on various materials, including from the Hong Kong Securities and Futures Commission (SFC) and the National Association of Financial Market Institutional Investors (China Bond Market Development Report 2011)

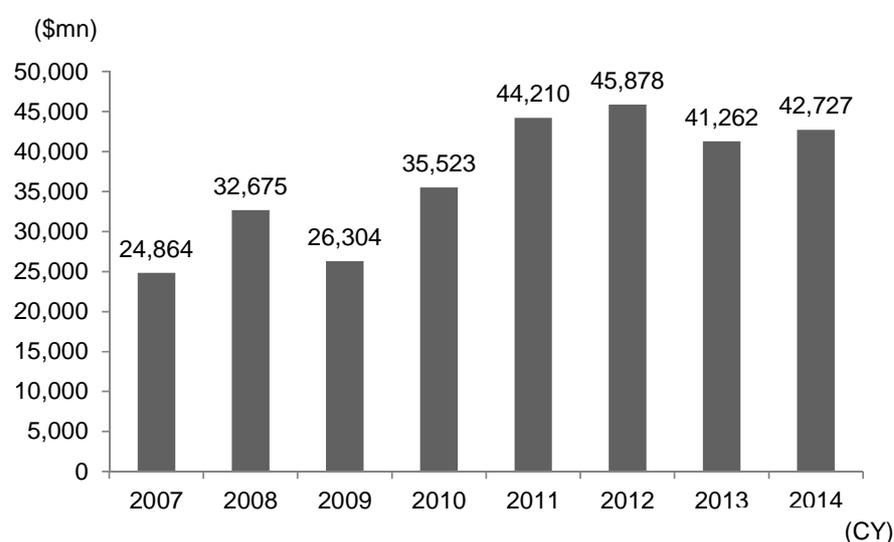
¹⁷ Sekine, E., *Chūgoku ni okeru hikyojūsha jinmingenken saiken (panda-sai) ichiba no genjō to kadai* [China's nonresident RMB-denominated bond (Panda bond) market: Current Status and Outstanding Issues], Nomura Capital Markets Quarterly, Summer 2006 (Japanese only).

4. Promotion of infrastructure imports

The establishment of the AIIB as a financial support for China's "One Belt, One Road" concept and development of the new Silk Road as well as the 2014 APEC summit meeting hosted by China, which took up the topic of global infrastructure development as one of its themes, has many participants in China's domestic market expecting domestic infrastructure-related companies to be major beneficiaries of the Chinese governments' push to develop infrastructure. This has given rise to (1) expectations of strong earnings at listed companies involved in such infrastructure-related areas as construction, electric power generation, electric power facilities, construction machinery, ports, railways, and airports, and (2) the emergence of an "overseas infrastructure construction concept stock" theme in China's equity market. In its 5 November 2014 issue¹⁸, the China Securities Journal referred to the Silk Road initiative as China's "Marshall Plan", the United States' plan for supporting the reconstruction of Western European countries after the Second World War. Under the Marshall Plan, U.S. lending of USD-denominated loans to Western European countries and the latter's purchase of goods from the United States helped establish the dollar as the world's core reserve currency.

A look at China's infrastructure-related exports shows the value of its exports of railway cars, airplanes, ships, and other transport equipment to the 57 founding members of the AIIB rose from about \$24.9 billion in 2007, prior to the global financial crisis, to over \$40 billion in 2011 (Figure 5).

Figure 5: China's infrastructure-related exports to AIIB member nations



Note: 1. Data based on value of China's exports of railway cars, airplanes, ships, and other transport equipment.

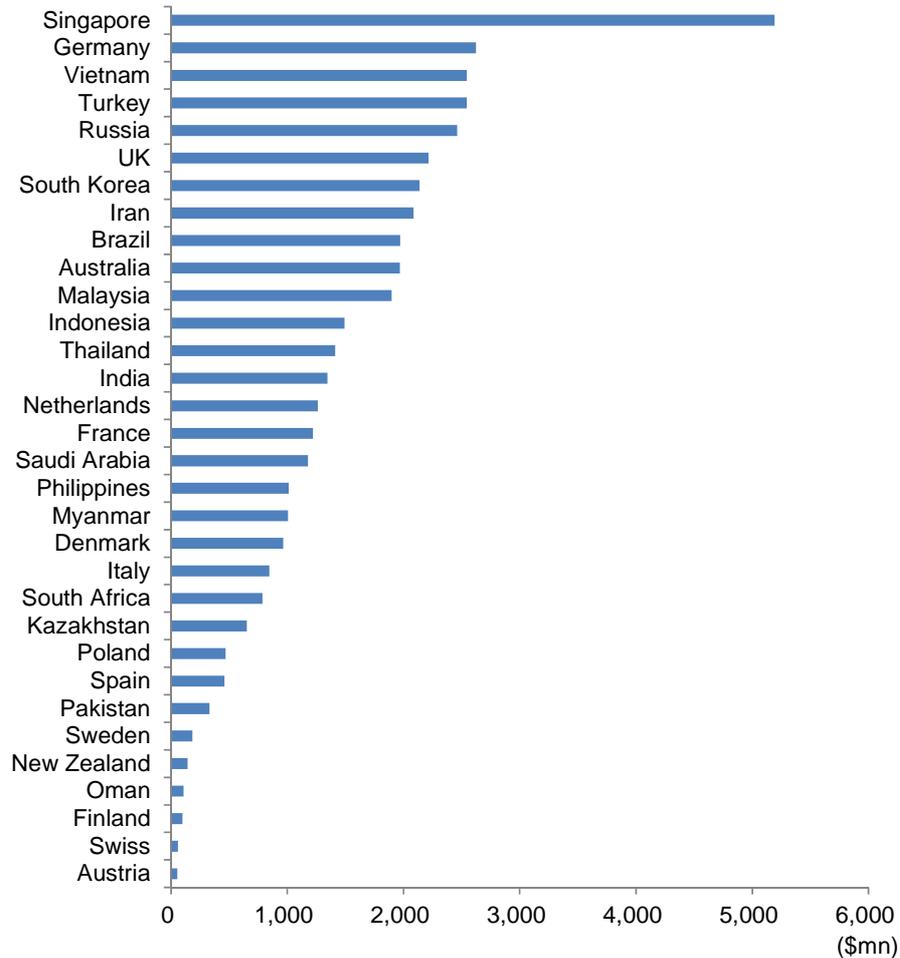
2. Based on exports to 32 nations included in China customs statistics.

3. Data for Oman included from 2012.

Source: Nomura Institute of Capital Market Research, from CEIC data

¹⁸ <http://www.stcn.com/2014/1105/11827922.shtml> (in Chinese)

**Figure 6: China's infrastructure-related exports to AIIB member nations
(by country, 2014 basis)**



Note: 1. Data based on value of China's exports of railway cars, airplanes, ships, and other transport equipment.

2. Based on exports to 32 nations included in China customs statistics.

Source: Nomura Institute of Capital Market Research, from CEIC data

Breaking down export value to these 57 nations by country (2014 basis), the top three importers of Chinese infrastructure-related goods are (1) Singapore (\$5.2 billion), (2) Germany (\$2.6 billion) and (3) Vietnam (\$2.5 billion) (Figure 6)¹⁹.

AIIB loans to Asian nations could add momentum to China's infrastructure-related exports, but a key concern for existing ADBs and related nations will be whether or not the conditions for AIIB loans will include a fairness rule related to the procurement of equipment and services, as is the case with loans from existing MDBs. Another key point will be ensuring that AIIB lending is made with due consideration for the environment and societal conditions and enhances the sustainability of economic growth in borrowing

¹⁹ On 28 October 2014, it was reported that China's two largest state-owned railcar makers, China South Locomotive & Rolling Stock Corporation Limited (CSR) and China CNR Corporation Limited (CNR) would merge. A few days earlier on 23 October, CNR won an order for its railcars from Boston's subway system, marking the first time a Chinese railcar maker received an order from the United States.

countries, as has been pointed out by Finance Minister Lou Jiwei. This is another area where the standards and rules of existing ADBs will be an important point of reference for the AIIB.

IV. Closing remarks

The establishment of the AIIB is expected to help meet the demand for funding of infrastructure development in the Asian region, but this demand cannot be met entirely by any single nation or MDB.

The joint statement released at the end of the APEC finance ministers' meeting held on 21 October 2014, shortly before the Beijing APEC summit meeting, states that "Given the large funding gap between projected infrastructure needs and limited financial resources of governments in the APEC region, we call for further efforts, including through our own policy reforms, to attract long-term financing and leverage private resource flows to fill the gap, including through public-private partnership (PPP)."²⁰ In addition to the negotiations over the AIIB's Articles of Agreement and the design of its governance systems, key points to watch for going forward include the mobilization of private-sector funds for infrastructure development in Asia and the reform of financial markets in Asian countries required to facilitate that mobilization.

Infrastructure development is also needed in China itself, and China's Ministry of Finance intends to promote infrastructure-related PPP. The "Beijing agenda" adopted at the Beijing APEC summit meeting also calls for the promotion of PPP in the Asian region²¹. Concerning the need for China to secure funding for its own infrastructure development, this author has previously recommended relaxing the regulations governing investment in domestic securities by qualified foreign institutional investors (QFIIs) and increasing the issuance of samurai bonds by Chinese issuers in the Tokyo market²². Looking ahead, the Asian nations are expected to hold multilayered discussions about the ideal means of securing funding for infrastructure development and then gradually shift to these new means of funding.

²⁰ http://www.mof.go.jp/international_policy/convention/apec/20141021.htm

²¹ http://www.mofa.go.jp/mofaj/ecm/apec/page22_001657.html

²² Sekine, E., *Ajia ni okeru infurafainansu ni muketa teigen* (Proposals for Financing Infrastructure in Asia), Chinese Capital Markets Research, Spring 2010 (Japanese only)