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## China's Instrument or Europe's Influence? Safeguard Policies in the AIIB

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### Global Development Finance

Multiple conflicts of interests exist in the international economic policy. In global development finance, industrialised countries often find themselves aligning while emerging and developing countries share common interests. At a time of power shift in the international system, while emerging and developing countries expand their economic and political influence, criticism on the existing international organisations and the call for reforms is growing (Czada et al., 2013, p. 589). The World Bank Group (WBG) is particularly active in international development cooperation, as are a large number of regional multilateral development banks (MDBs). These MDBs are mostly very similar in structure to the WBG lead International Bank for Reconstruction and Development (IBRD). However, within this current system emerging and developing countries regard their interests as not sufficiently taken into account. They criticise the system of international development banks for the distribution of votes, which no longer corresponds to the distribution of power in the international system. A further criticism is an intervention by international organisations in the sovereignty of borrowing countries (Wang, 2017, pp. 113–116). In order for a project to be financed by many MDBs, standards, in particular environmental and social standards (safeguards), must be met. With these safeguards, the bank aims to ensure the effectiveness and sustainability of the financed projects (Humphrey, 2016, p. 2). Consequently, through financing projects, the WBG pursues to bring about social and political change in the borrowing countries (Wang, 2017, pp. 113–116).

The criticism of the current international economic system is growing. However, since reforms proceed too slowly or fail altogether, emerging and developing countries consider establishing alternative institutions. Consequently, at the initiative of China a new MDB, the Asian Infrastructure Investment Bank (AIIB), was founded as a rival to the WBG (Varwick & Woyke, 2015, p. 551). Therefore, the AIIB is expected to differentiate from the IBRD and similar MDBs to meet the critique. Nevertheless, the AIIB has introduced safeguards policies and established in 2016 its "Environmental and Social Framework". One year earlier than the AIIB, the New Development Bank (NDB) was founded by the BRICS countries (New Development Bank, 2014, para. 1). The NDB and the AIIB share many similarities. However, in contrast to the AIIB, the NDB does not admit to safeguards. How can it be explained that the AIIB, founded as a competitor to the WBG on the initiative of China, is committed to environmental and social standards? This question is in the following empirically and theoretically examined through a congruence analysis. Therefore, first, the motivations, structure, and principles of the AIIB are briefly introduced. This is followed by outlining possible explanations from the perspective of the three theories of International Relations 1) neorealism, 2) neoliberal institutionalism, and 3) social constructivism, whereby the focus is set on the studying China's behaviour.

### The AIIB and the Introduction of Safeguard Policies

The establishment of the AIIB and the NDB has triggered a debate on safeguard policies, criteria in development finance (Esteves et al., 2016, p. 6), and their role in the international economic system (Wang, 2017, p. 113). In 2015, the AIIB was founded to promote infrastructure investment in Asia (Asian Infrastructure Investment Bank, 2015, para. 1). The bank has 57 founding members, including numerous non-regional members, also European countries (Bundesministerium der Finanzen, 2016, pp. 29–30). An endeavour behind the foundation of the AIIB was to reform

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the current system of financial governance, in particular, the distribution of votes in international organisations. Additionally, national interests constitute a further motivation behind the establishment of the AIIB. Thereby, China's motivation is in the focus since the country can expand its influence through the AIIB (Wang, 2017, p. 114).

However, in order to assess the potential influence of the AIIB in the system of international development finance, it is necessary to assess its financial resources. At the beginning of 2016, the AIIB owned a capital stock of 100 billion dollars, of which 20 billion dollars are paid-in shares (Asian Infrastructure Investment Bank, 2015, para. 4 (1,2)). The subscribed capital of the IBDR amounted to 279.9 billion US dollars in mid-2019, but the paid-in capital reached only 17.1 billion US dollars (The World Bank, 2019, p. 82). China has with more than 26% the highest percentage of votes in the AIIB (Asian Infrastructure and Investment Bank, 2020), and thus exceeds the United States' (US') voting share in the IBRD, which account for 15.76% (Secretariat, 2020). In the AIIB China is the only member with a veto right (Asian Infrastructure Investment Bank, 2015, para. 28 2 ii). The AIIB states that the bank and its staff should not interfere in the political affairs of member states through their activities. The principle is that only economic considerations should be taken into account in their decisions (Asian Infrastructure Investment Bank, 2015, para. 31 2). This represents a difference to the WBG's ideas (Wang, 2017, p. 116). Nevertheless, in 2016, the AIIB announced its policy and standards. In its overarching policy, the AIIB outlines:

"The Bank recognizes that environmental and social sustainability is a fundamental aspect of achieving outcomes consistent with its mandate to support infrastructure development and enhance interconnectivity in Asia. The objective of this overarching policy is to facilitate achievement of these development outcomes, through a system that integrates sound environmental and social management into Projects" (Asian Infrastructure Investment Bank, 2019, p. 7).

## **Explanation from the Perspective of Neorealism**

The theory of neorealism describes the international system as anarchically structured. According to Waltz, the structure of the international system is responsible for states' behaviour. Every state strives for a gain of power and aims to ensure its survival as a sovereign state. The more power a state has in comparison to other states, the more secure it is to assert its interests. Thus, other national interests are subordinated to security policy objectives (Varwick & Woyke, 2015, p. 397). States all act according to their self-interest and try to gain an advantage over others. Although states cooperate with each other, this cooperation has limitations and can only be temporary since states attempt to avoid dependencies (Mearsheimer, 1994, pp. 9–13). Against the background of neo-realism, it can be hypothesised that China's gained power through the foundation of the AIIB is the reason for the introduction of safeguards in the bank.

The AIIB was founded at a time of power shifting in the international system (Wang, 2017, p. 114). While the US still has a dominant position in international organisations, the international system is becoming more complicated (Hopewell, 2016, p. 205). In this context, the AIIB is perceived as competing against the US-dominated Bretton Woods institutions (Varwick & Woyke, 2015, p. 551) and is expected to have together with the NDB a lasting impact on the global development finance (Reisen, 2015, p. 274). In addition to promoting international financial stabilisation and growth in emerging and developing countries, development banks are committed to follow national interests and disseminate political views of their most influential member states (Liao, 2015, p. 1).

The goal of China is to reduce the hegemonic power advantage of the US. China has a leadership position in the AIIB (Humphrey, 2016, p. 29) and ensures that it is the largest shareholder in terms of voting right and financial resources (Liao, 2015, p. 3). Consequently, the neorealist approach explains the introduction of safeguards in the AIIB as a purely rational behaviour of China. The safeguards offer an instrument for China to pursue its goals more successfully. Safeguard policies made it possible to persuade important European countries, such as France and Germany, to join the AIIB (Wang, 2017, p. 114). The positive consequences of a membership of several European countries are more capital, a very good credit rating, and a strong position in the international system (Humphrey, 2015, p. 6). At the same time, abandoning safeguards in the NDB shows that these standards are to China itself not relevant. Another argument for China's purely strategic approach with the goal of power-gain is China's pretence of reforming the international system by empowering emerging and developing countries (Humphrey, 2016, p. 1). The

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distribution of votes within the AIIB adds to China's influence, but not directly to the influence of emerging and developed countries in general (Asian Infrastructure and Investment Bank, 2020). Furthermore, China pursues the objective of promoting its Belt and Road Initiative. By building AIIB infrastructure projects along these routes, China can expand its geopolitical and geo-economic dimensions of power (Wilson, 2017). Additionally, not only does the AIIB help China to gain more power internationally, but also to gain influence in the borrowing countries at the regional level.

In general, the neorealist approach manages to explain the introduction of safeguard policies in the AIIB. However, the realist understanding of cooperation in alliances is problematic since the AIIB is not an alliance which is essential to survive. Moreover, from a neorealist perspective, the membership of European states in the concurrence organisation to Western dominated international organisations is inconsistent. For the neorealist explanation, economic, social, and cultural factors do not matter (Varwick & Woyke, 2015, p. 400). However, China's gain of power is predominantly measured through its economic growth. Consequently, the economic factor seems important to consider.

## Explanation from the Perspective of Neoliberal Institutionalism

Unlike neo-realism, neoliberal institutionalism assumes that the two core problems of anarchy, insecurity and market failure, can be overcome through interdependence and institutions (Schimmelfennig, 2015, p. 112). As a result, states can strive for other goals than the gain of power and instead for absolute profits (Schimmelfennig, 2015, pp. 95–97). States join institutions from which they expect a greater advantage than costs. Thus, international organisations have the function to reduce uncertainty (Keohane, 1982, pp. 331–346). Neoliberal institutionalism hypothesises that China's economic interests are the reason for the adoption of safeguard policies in the AIIB.

China and the West share a strong economic interdependence (Varwick & Woyke, 2015, p. 13). As a consequence of international interdependence, states rely on other states for achieving their goals. Without cooperation, goals can only be reached less efficiently. Therefore, the AIIB is an answer to the increasing interdependence between China and the West since the cooperation enables a more efficient development financing. China regards the AIIB as an opportunity to increase the efficiency of its investments in domestic and foreign infrastructure projects. The AIIB, as a competitor to the IBRD and other MDBs, can contribute to structural reforms and increase efficiency (Wang, 2017, p. 116). Many countries lack development finance, with, in particular, a gap in infrastructure investment (Humphrey, 2016, p. 3). Furthermore, China is interested in profitable foreign investment, and the Chinese economy should be further internationalised (Ferdinand, 2016, pp. 951–952). Since China's economy depends on exports, the state has a great interest in a growing world market and seeks to improve access to foreign markets (Hopewell, 2016, p. 125). Additionally, is China's economy undergoing a transformation from a manufacturing to a service economy, which will increase the country's goods import over the next decades. This need is to be covered especially by Southeast Asian countries (Liao, 2015, p. 5).

The AIIB leads to absolute profits for China. The economic interests are decisive. A concrete example for Chinese economic interests is the Belt and Road Initiative, whereby China is following the goal of expanding its trade and foreign investment (Wang, 2017, p. 117). Numerous AIIB projects are infrastructure projects along the Belt and Road routes (Wang, 2017, p. 116). China also hopes to promote the internationalisation of its currency and thereby to reduce its dependence on the US' currency (Wang, 2017, p. 114). A large number of member states in the AIIB, including numerous countries with good credit ratings, make that AIIB have already more capital than other MDBs and an AAA rating (Humphrey, 2016, iii).

China can draw numerous absolute profits from the AIIB, which represent an opportunity for the infrastructure development of Asia and thus also for the economic development of China. The introduction of environmental and social standards in the AIIB is thus assessed by the theory of neoliberal institutionalism as China's instrument to promote the expansion of cooperation. Safeguards have been relevant for the membership, especially of European countries. China has subsequently agreed to enshrine such standards in the AIIB's structure (Humphrey, 2016, p. 26). From an institutionalist approach, the bargaining power of European AIIB founding members can explain the implementation of safeguards. The states' bargaining power determines which specific rules are agreed on and how

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the profit is distributed (Schimmelpfennig, 2015, p. 257). China, as the initiator of the AIIB, has divorced itself from its leadership role and is, thereby, making membership more attractive to other countries (Humphrey, 2016, p. 26).

## **Explanation from the Perspective of Social Constructivism**

Constructivism regards the international system as socially structured. Ideas, such as knowledge, political values, and norms, are important for the international system, as well as are the identity, resulting culture, and community. The actors act according to the logic of appropriateness and social conformity (Schimmelpfennig, 2015, pp. 161–165). For international cooperation, the degree of idea convergence is crucial (Schimmelpfennig, 2015, p. 185). Thus, similarities constitute a prerequisite for cooperation in international politics (Schimmelpfennig, 2015, pp. 168–169). The social constructivist approach hypothesis articulates China's learning and socialisation process initiated by the European states as the reason why the AIIB has introduced safeguard policies.

In order to facilitate cooperation within the AIIB, a common idea of development financing is required. The European community characterises a common culture with shared knowledge, values, and norms (Schimmelpfennig, 2015, p. 165; Stratschulte, 2014, pp. 173–175). Therefore, the members of a community expand their culture through socialisation (Schimmelpfennig, 2015, p. 161). A learning and socialisation process of China results in a growing integration into the Western order (Varwick & Woyke, 2015, p. 13). Hence, international socialisation is a central process of international politics through which actors become members of a community. Knowledge, values, and norms are internalised and adopted as an actor's own identity. In that, actors' argumentative power, which is influenced by the credibility of the arguments and whose political goals are closer to the ideas of the community, shapes the results (Schimmelpfennig, 2015, p. 179). International communities attempt to find new supporters for their ideas (Schimmelpfennig, 2015, pp. 173–174), whereby standards are crucial for the common idea (Schimmelpfennig, 2015, pp. 164–165).

China has, thus, recognised the knowledge of the importance of safeguard policies for the efficiency of the AIIB. Additionally, the high level of international legitimacy is crucial for the adoption of ideas (Schimmelpfennig, 2015, p. 175). Social constructivism, therefore, explains the introduction of the environmental and social standards in the AIIB with the argumentative power of the European states. The European states have been able to successfully justify their values and convincingly communicate their ideas on the relevance of safeguards. Consequently, China accepted safeguard policies within the AIIB. This kind of structural change can take place in the international system as cognitive learning leads to a change in inter-state relations. A change in the view or behaviour of the Chinese leadership may have ideological, legitimacy or economic reasons. The cost of change or adjustment is below the resulting gain (Weithas, 2012, pp. 87–88).

Therefore, for China, the benefits of establishing the AIIB with many member states and several major European countries appear greater than the cost of adaptation and the socialisation process (Schimmelpfennig, 2015, p. 127). Although China recognises the standards within the AIIB, the socialisation's impact is rather low. The Chinese state has not internalised these values and ideas so far that the Chinese state would insist on introducing safeguard policies within the NDB. Therefore, it is questionable whether China has an interest in these values, ideas, and the process of learning and socialisation, or whether China is accepting standards, like neo-realism and neo-liberal institutionalism point out, as an instrument.

## **Conclusion**

All three International Relations theories, in general, manage to explain the introduction of safeguard policies in the AIIB. Neorealism declares this process with a power-gain for China through the AIIB. The standards are for China an instrument which enables the membership of European countries in the AIIB and, thus, increases the influence and significance of the development bank. Neoliberal institutionalism outlines China's economic interests as the reasons for safeguards in the AIIB. The strong economic interdependence, as well as China's objective to further develop the cooperation with European states, have led to the introduction of safeguard policies. Thus, China has adopted ideas and values which were enforced by European states through their argumentation power. However, explaining the introduction of safeguards merely through China's expansion of power over the US or with China's learning process

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seems to be a too narrow consideration. Therefore, the most comprehensive explanation is provided by the neoliberal institutionalist approach, which traces China's behaviour back to the pursuit of absolute gains. China has an interest in cooperating because this can increase efficiency and help to internationalise the Chinese economy. The concession of environmental and social standards in the AIIB makes extended cooperation with European states possible and, thus, represents an instrument of China. Furthermore, it appears plausible that in addition to economic interests, the neorealist idea of China's expansion of power besides plays a role in the international system. This is connected to China's goal to gain more influence and enforce national interests more successfully. The rise of China is an important question for the future, as it changes international politics and the structure of the global economy. China can increasingly use its economic power to pursue political goals in the international system. "Thus, the West faces the challenge of rethinking the relationship between politics and business in the global context" (Varwick & Woyke, 2015, p. 551). However, in the end, the AIIB's safeguard policies might lead to a bureaucratic system similar to the IBRD and other traditional MDBs, creating a development bank that does not match what China has been aiming for (Humphrey, 2015, p. 2). It is not yet clear how the AIIB will develop and how it will continue to differentiate itself from other development banks as it faces the same challenges as the WBG and other MDBs (Humphrey, 2015, iii).

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