Scaling up Finance for the Sustainable Development Goals: The role of development banks

Daniel Poon, Economist

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“Money, finance and debt: Old debates, new challenges”
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Over 70 years since Bretton Woods: New Players in Development Banking

BRETTON WOODS MONETARY CONFERENCE

In 1944 the United States government chose the Mount Washington Hotel as the site for a gathering of representatives from 44 countries. This was to be the famed Bretton Woods Monetary Conference. The Conference established the World Bank, set the gold standard at $35.00 an ounce, and chose the American dollar as the backbone of international exchange. The meeting provided the world with a badly needed post-war currency stability.

THE OPENING CEREMONY OF THE ASIAN INFRASTRUCTURE INVESTMENT BANK

January 16th, 2016 Beijing, China
2016年1月16日 中国·北京

Ceremony of The New Development Bank
Outline of presentation

1. Comparing new MDBs: AIIB and BRICS bank
2. Some features of new MDBs
   i. China’s experience in national development banks (NDBs)
   ii. Potential role of ‘special fund’ mechanism
3. China’s overseas investment funds
4. What makes new MDBs different from existing MDBs?
5. Conclusion: achievement of SDGs?
Addis Ababa Action Plan

On bridging the infrastructure gap:

- Main outcome was to establish “global infrastructure forum”, to meet periodically to improve alignment and coordination among established and new infrastructure initiatives.

- For example, the World Bank’s Global Infrastructure Facility (GIF) has total funding size of $84.4 million.

- But, China is the largest contributor with $20m.

- Other main contributors are: Australia ($18.6m), Canada ($15.8m), World Bank ($15m), and Japan ($15m).
# 1. Comparing New MDBs

<table>
<thead>
<tr>
<th></th>
<th>New Development Bank</th>
<th>AIIB (Asian Infrastructure Investment Bank)</th>
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</thead>
<tbody>
<tr>
<td><strong>Official Launch</strong></td>
<td>July 2015</td>
<td>January 2016</td>
</tr>
<tr>
<td><strong>Headquarters</strong></td>
<td>Shanghai</td>
<td>Beijing</td>
</tr>
<tr>
<td><strong>Largest Shareholder</strong></td>
<td>Equal among BRICS</td>
<td>China (32%)</td>
</tr>
<tr>
<td><strong>Credit Rating</strong></td>
<td>AAA (domestic, China)</td>
<td>AAA (international)</td>
</tr>
<tr>
<td><strong>Total Lending ($billions)</strong></td>
<td>3.4</td>
<td>4.2</td>
</tr>
<tr>
<td><strong>Total Number of Projects</strong></td>
<td>13</td>
<td>24</td>
</tr>
<tr>
<td><strong>Member Countries</strong></td>
<td>5</td>
<td>84</td>
</tr>
<tr>
<td><strong>Countries Invested</strong></td>
<td>5</td>
<td>12</td>
</tr>
<tr>
<td><strong>Target Sectors (% value)</strong></td>
<td>Renewable energy and environmental (74%)</td>
<td>Infrastructure (100%) of which: energy (45%)</td>
</tr>
<tr>
<td><strong>Staff (# people)</strong></td>
<td>130 (end-2017)</td>
<td>100 (end-2016)</td>
</tr>
<tr>
<td><strong>Authorized capital ($bn)</strong></td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td><strong>Subscribed capital ($bn)</strong></td>
<td>50</td>
<td>-</td>
</tr>
<tr>
<td><strong>Callable capital ($bn)</strong></td>
<td>40</td>
<td>80</td>
</tr>
<tr>
<td><strong>Paid-in capital ($bn)</strong></td>
<td>10</td>
<td>20</td>
</tr>
</tbody>
</table>
2. Some Features of New MDBs

- Existing studies estimate lending scale of new MDBs by generalizing assumptions based on operations of existing MDBs.

![Figure 5. Likely Scenarios of BRICS NDB Loan Portfolio, 2016–2025](image1)

![Figure 7. Likely Scenarios of AIIB Loan Portfolio, 2016–2025](image2)

Source: Calculations by Judith Tyson, ODI
i. China’s Experience with CDB

- Mid-1990s, CDB was bailed-out in late-1990s. Today, it is world’s largest national development bank (by assets), and China’s largest bank for foreign investment and financing
- CDB benefits from high-grade country credit rating, and implicit guarantee from government
- CDB issues long-term bonds purchased by state-owned banks that consider them as assets with ‘risk-free’ returns on depositors’ funds
- Chinese policy-makers often invoke the term “exploration” (*tansuo* 探索) to explain their experience in domestic development finance
# Loan-to-Equity Ratios, Selected MDBs

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</thead>
<tbody>
<tr>
<td>AfDB</td>
<td>1.6</td>
<td>1.7</td>
<td>1.9</td>
<td>2.0</td>
<td>2.0</td>
<td>2.1</td>
<td>2.0</td>
<td>n/a</td>
<td>1.9</td>
</tr>
<tr>
<td>ADB</td>
<td>2.6</td>
<td>2.7</td>
<td>2.8</td>
<td>3.0</td>
<td>2.9</td>
<td>3.1</td>
<td>3.3</td>
<td>3.6</td>
<td>3.0</td>
</tr>
<tr>
<td>CAF</td>
<td>n/a</td>
<td>n/a</td>
<td>2.3</td>
<td>2.4</td>
<td>2.3</td>
<td>2.2</td>
<td>2.1</td>
<td>2.1</td>
<td>2.2</td>
</tr>
<tr>
<td>EIB</td>
<td>5.3</td>
<td>5.7</td>
<td>5.7</td>
<td>5.4</td>
<td>5.2</td>
<td>5.6</td>
<td>5.2</td>
<td>5.4</td>
<td>5.4</td>
</tr>
<tr>
<td>World Bank (IBRD)</td>
<td>2.9</td>
<td>3.3</td>
<td>3.4</td>
<td>3.6</td>
<td>3.6</td>
<td>3.8</td>
<td>3.9</td>
<td>4.3</td>
<td>3.6</td>
</tr>
</tbody>
</table>

*Source: Authors’ elaboration based on balance sheets’ information from MDB annual reports.*
Loan Levels and Gearing Ratios: Selected MDBs and NDBs
ii. AIIB Special Fund Mechanism

AIIB’s articles of agreement permit, by super majority vote, a max. gearing ratio of **2.5** of the bank’s “unimpaired subscribed capital, reserves and retained earnings included in its ordinary resources”

- Article 10 mentions that Bank operations consist of two types:
  1) Ordinary operations financed from **ordinary resources**;
  2) Special operations financed from **special funds resources**

- These two types of operations may separately finance elements of the **same** project or program
- (this provision not found in BRICS Bank AoA)
- Remainder of Article 10 establishes clear partition between ordinary resources and special funds resources
Tapping Domestic and International Capital Markets?

- AIIB’s institutional design appears to maintain a *de jure* loan-to-equity ratio aimed at safeguarding access to international capital markets.
- Also creating a conduit that – in indirectly tapping China’s domestic capital markets – allows for *de facto* infrastructure financing to be scaled-up above the statutory limit.
- (AIIB planned its first international bond issuance in the second quarter of this year)
- China has also established a growing number of purpose-built national, regional and bilateral investment funds to provide equity financing.
### 3. Selected China National, Bilateral, and Regional Investment Funds

<table>
<thead>
<tr>
<th>Name</th>
<th>Established</th>
<th>Scale ($bn)</th>
<th>Chinese Investors</th>
<th>Other Investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>China-Africa Development Fund</td>
<td>2007</td>
<td>10</td>
<td>China Development Bank (CDB)</td>
<td>-</td>
</tr>
<tr>
<td>China-ASEAN Investment Cooperation Fund</td>
<td>2013</td>
<td>10</td>
<td>China Export-Import Bank (EXIM)</td>
<td>-</td>
</tr>
<tr>
<td>China-Central and Eastern Europe Investment Cooperation Fund</td>
<td>2013</td>
<td>1</td>
<td>China Exim</td>
<td>Hungarian Export-Import Bank</td>
</tr>
<tr>
<td>Silk Road Fund (SRF)</td>
<td>2014</td>
<td>40</td>
<td>SAFE, CIC, EXIM, CDB</td>
<td>-</td>
</tr>
<tr>
<td>China-Kazakhstan Production Capacity Investment Fund</td>
<td>2015</td>
<td>[2]</td>
<td>SRF</td>
<td>-</td>
</tr>
<tr>
<td>China-LAC Cooperation Fund (Private Equity Fund)</td>
<td>2015</td>
<td>3</td>
<td>EXIM</td>
<td>-</td>
</tr>
<tr>
<td>China-LAC Industrial Cooperation Investment Fund (CLAIFUND)</td>
<td>2015</td>
<td>10</td>
<td>SAFE, CDB</td>
<td>-</td>
</tr>
<tr>
<td>China-Africa Production Capacity Cooperation Fund</td>
<td>2016</td>
<td>10</td>
<td>SAFE, EXIM</td>
<td>-</td>
</tr>
<tr>
<td>China-Russia Regional Development Investment Fund</td>
<td>2017</td>
<td>15.4</td>
<td>National Development and Reform Commission (NDRC)</td>
<td>-</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td></td>
<td><strong>99.4</strong></td>
<td></td>
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</table>
4. What makes new MDBs different?

At signing ceremony for the New Development Bank HQ, then-Finance Minister Lou Jiwei outlined 5 types of “innovations” needed for multilateral development banking for the 21st century:

i. **innovative development thinking**, that supports countries in pursuit of their own development models and greater South-South experience sharing;

ii. **innovative business models**, that provide developing countries with custom-tailored support in finance, technology and knowledge;

iii. **innovative organizational structures**, that are fit-for-purpose, allowing flexible and efficient operational procedures;

iv. **innovative financing tools**, that expand financing channels;

v. **innovative development practices**, that treat development as a dynamic process
• **AIIB’s Jin Liqun:** “We must have creative spirit, and neither clone the World Bank nor copy the ADB.”

• Signals that Chinese policy-makers seek to experiment with long-term non-concessional development finance

• **PBoC Zhou Xiaochuan:** positioned the role of development finance as in between that of concessional and commercial finance, but “slightly tilted” toward the latter

• Not inconceivable that these various vehicles could selectively finance AIIB infrastructure projects through the special funds mechanism

• Especially as the Bank garners further expertise managing projects in different regional contexts
Conceptual Infrastructure Project Financing Structure

- **CDB** – debt financing
- **Exim Bank** – debt financing
- **CIC** – further equity financing
- **SRF and other public/private investors** make joint equity investment in a project
- **AIIB**, further support by arranging initial debt financing
- **BRICS Bank (?)**
- **Other China overseas investment funds** (via special funds mechanism)
Policy vs. Project Conditionality

- No signs, thus far, that China is willing to engage in *policy conditionality* linked to overseas financing.
- IMF/WB policy conditionality not part of China’s own development experience.
- Different approaches to mobilizing private sector finance:
  - **WB’s cascade/blended finance** approach, first seeks to mobilize commercial finance enabled by “*upstream reforms* where necessary to address market failures and other constraints to private sector investment at the country and sector level”.
  - **AIIB** will “prioritize potential investments and sectors *based on their readiness* for private sector investment, regulatory regime and contractual arrangements, among other factors. The Bank will identify transactions where its public sector relationships can enable success, and success can be replicated.”
AIIB: no Chief Economist

AIIB Organizational Structure

Jan. 8, 2018
5. Conclusion: achievement of SDGs?

- Larger context of Belt & Road Initiative, as China’s foreign economic policy (AIIB and BRI are not the same but significant overlap)
- In July, US announced “Indo-Pacific Economic Vision” to increase financing to countries in the region with $113m in direct government investment, bolstered by investment agreement among US, Japan, and Australia
- Financial support also from proposed US development finance reorganization and to double spending cap to $60bn for loans for US firms investing in overseas projects
- Consolidation of Overseas Private Investment Corp. (OPIC), the Development Credit Authority (DCA) of the US Agency for International Development (USAID); to create a new institution, US International Development Finance Corp. (IDFC)
- Competition with China, appears to be a prominent driver of US interest in development finance reform