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# Creation of the Asian Infrastructure Investment Bank as a part of China's smart power strategy

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## ABSTRACT

The aim of this article is to assess the creation of the China-led Asian Infrastructure Investment Bank within the scope of China's smart power strategy, which will help not only to analyze China's strategic use of its coercive and co-optive capacity, but also to understand better the concept of smart power. Given that the wisdom of statecraft can only be situationally determined, through this study I will propose the ability to achieve targeted objectives, the skill to use hard and soft power instruments in such a way that they reinforce each other, good interpretation of the existing regional and global contexts, time planning, and compatibility with long-term interests as criteria for judging the effectiveness of a smart power implementation.

**KEYWORDS** Asian Infrastructure Investment Bank; China; one belt one road; smart power; soft power

## Introduction

Power is a central and widely used concept in international relations (IR); however, its elusive nature and difficulty to measure make it difficult to ensure consensus on a common definition. Morgenthau (1964, p. 27) states that 'the concept of political power poses one of the most difficult and controversial problems of political science'. Almost all of the different schools of IR theory deal more or less with this fundamental concept in the study of world politics, and scholars from these schools of thought use and interpret this concept in their own way. It is common among them to define power using related terms such as influence, control, coercion, or force. Hence, the concept of power is the subject of many studies that aim to define better its nature and its role in IR, such as structural power (Strange, 1988), normative power (Manners, 2002), soft power (Nye, 2004), smart power (Nossel, 2004) and compulsory power (Barnett & Duval, 2005).

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Smart power, which is a relatively new output of such studies, is the main focus of this article. Coined by Suzanne Nossel and developed by Joseph Nye, smart power is defined as the ability to combine hard and soft power into a successful strategy (Nye, 2011, p. 23). The George W. Bush administration's war on terrorism showed that hard power does not necessarily translate into *influence*<sup>1</sup> in today's world, and it may even undercut soft power, tarnishing the US' image due to the illegal war in Iraq and the unlawful treatment of prisoners. This situation thus revealed the necessity for the smart use of power resources.

Although the concepts of hard power and soft power have been largely explored, comprehensive studies devoted directly to the concept of smart power are still limited in number and scope. Nye (2011), Wilson (2008), Cross (2011), and Gallarotti (2015) are the main scholars who have written about this concept directly. Despite the fact that the concept is increasingly used in high-level speeches (see especially Clinton, 2009; Rehn, 2008; Richardson, 2008; Waldner, 2007), academic research on the meaning and practices of this concept is still lacking. Consequently, it is still difficult to assess 'how much substance does it really have, and whether the concept has any place in long-standing scholarly debates about power' (Cross, 2011, p. 692). Besides, one of the main shortcomings of the research conducted so far on smart power is case selection, as the aforementioned scholars have analyzed this concept in the context of the US or Europe.

Since the wisdom of statecraft can only be situationally determined, different case studies providing an analysis of the practice of smart power would contribute not only to filling the gap in the existing literature, but also to evaluating the concept of smart power. Based on this assumption, in this article I aim to analyze smart power in the context of Chinese foreign policy, and more particularly to answer the question of whether the formation of the Asian Infrastructure Investment Bank (AIIB) can be assessed as a part of China's smart power approach to advancing Chinese national interests. To this end, I propose five criteria for assessing 'smartness': the ability to achieve targeted objectives; the skill to use hard and soft power instruments in such a way that they reinforce each other; good interpretation of the existing regional and global contexts; time planning; and compatibility with long-term interests. I argue that the launch of the AIIB is an ideal case through which to examine China's smart power approach, since it represents a strategic calculation that Beijing has long-term interests in combining its economic capabilities (economic carrots) and its preference for multilateralism and regional development (soft power resources) in order to attain its goals and fulfill its national interests.

Using an analytical method, I will first touch on the two components (hard and soft power) of the concept of smart power in the Chinese

context. Then, I will analyze the concept of smart power, recombining its two components to understand better the nature and the dynamics of smart power, and proposing various criteria for judging the smartness of a foreign policy action. Finally, dealing with the formation of the AIIB as a case study through which to analyze China's smart power strategy, I intend to provide useful information about China's way of using its power resources, its preferences in terms of power behavior, and its foreign policy moves.

## Two forms of power with Chinese characteristics

Before elaborating on the concept of smart power, it would be useful to unpack conceptually the two components of smart power in the Chinese context. China's rise on the world stage has been largely due to its economic progress over the course of the last three decades and its concomitant military capabilities, demonstrating that 'economic wealth and military power become increasingly synonymous' (Gilpin, 1981, p. 124). Hence, China has considerable potential to exercise hard power through a sticks and carrots approach. Although the Chinese leadership is trying hard to convince the international community that it will remain committed to a 'peaceful development', a 100-year long humiliating experience in its modern history proved to the Chinese political elites the importance of hard power. 'The Chinese slogan *'guojia zunyan shi da chulai de'* (national respect can only be obtained through fighting) illustrates the wisdom gained from this experience' (Jia, 2010). As a result, fueled by remarkable economic growth and a will to secure its national interests, China has embarked on an ambitious military build-up. Today, China's huge military spending, investment in military capabilities and efforts for military modernization are the main sources of the international debate over whether China's rise will be peaceful or threatening. The 1995–1996 Taiwan Strait Crisis, Chinese warships sailing near the disputed Senkaku/Diaoyu Islands, Chinese naval patrols in the disputed waters of the South China Sea, and the Scarborough Shoal standoff between China and the Philippines in 2012, demonstrate that Beijing does not hesitate to use military power to protect its interests, although it avoids being involved in military conflicts.

As for the economic part of hard power, China's huge impact on the global economy due to its present level of economic growth, production, trade, consumption, and capital movements provide Beijing with an undeniable economic power which goes hand in hand with political influence. Taking advantage of the asymmetrical economic interdependence in its favor, China successfully uses the sticks and carrots approach. For instance, Beijing provides aid to Pacific nations on the condition that they

recognize the People's Republic of China as the legitimate government of China and not Taiwan. The rare earth element embargo against Japan after the 2010 Senkaku/Diaoyu Islands incident, China's January 2010 statement threatening sanctions on US defense companies that sell arms to Taiwan, banana restrictions, and the tourist advisory statements against the Philippines after the 2012 Scarborough Shoal standoff, are other examples of China's use of economic hard power.

Along with hard power, China also invests heavily in soft power in order to counteract the 'China threat' theory, assuring other countries that its rise will be peaceful, and to secure resources and markets that support its economic growth. It is worth noting that soft power is not an unfamiliar concept to the Chinese political elites, as there are similarities between ancient Chinese thought and this concept. For instance, Sun Tzu (554-496 BC) advocates winning a battle without a fight, while Confucius (551-479 BC) suggests that a ruler should win the allegiance of the people with virtue, not by force (Fan, 2008, p. 3). On this basis, the interest of the People's Republic of China in soft power started developing in the 1990s, and the projection of soft power was identified as the dominant state policy after the 17th National Congress of the Communist Party of China in 2007.

The concept of soft power has become a hot topic in China as well as abroad (see especially Breslin, 2011; Gill & Haung, 2006; Glaser & Murphy, 2009; Kurlantzick, 2007; Li, 2008), due to the expansion of China's soft power influence around the world. The soft power discussion among Chinese scholars has revealed two main schools of thought: the culture school, which considers China's ancient history and traditional culture as the main source of its soft power; and the politics school, which focuses on China's political power, such as its ability in international institution building, agenda setting and mobilization of coalitions (Glaser & Murphy, 2009, p. 16-17). The former perceives China's cultural elements, such as Confucian heritage, which creates a common cultural sphere in East Asia, Chinese Marxism, identified as the backbone of the Chinese economic miracle, traditional Chinese medicine, and martial arts, as the core of China's soft power. The latter prioritizes China's foreign policy initiatives, such as good neighborhood diplomacy, public diplomacy, participation in UN peacekeeping operations, and overseas assistance programs.

As a result, China benefits from various tools which serve to enhance its global image and influence, such as the Confucius Institutes established all over the world in order to promote Chinese culture and language, a strong media campaign via the first 24-hour English-language news channel (CNC World), high level visits on bilateral and multilateral levels, and active engagement with international institutions and organizations, e.g. ASEAN +3, the East Asia Summit, the World Trade Organization and the Shanghai

Cooperation Organization. In terms of political values, China opts to promote its own values and principles such as global harmony, non-interference in internal affairs, and peaceful coexistence, rather than the allegedly universal values such as democracy and the human right of freedom of speech, with the intention of being able to compete with the US, a powerful proponent of these values, for global influence. The Chinese model of development - economic liberalization without political liberalization - offers developing countries an alternative to the Washington Consensus, challenging US values. This model, attracting the interests of countries from Africa, Latin America and Asia, contributes significantly to China's soft power.

Although soft power resources tend to be associated with intangible resources (culture, foreign policy, and political values), this does not mean that military force and economic might cannot produce soft power. For instance, today China is one of the largest contributors to UN peacekeeping forces, deploying 2436 troops, 30 military experts and 175 police for a total of 2639 personnel, according to the UN statistics of August 2016 (Blasko, 2016, p. 3). The other example of China's use of economic instruments to foster soft power is economic diplomacy, including foreign aid, donations and development assistance. China is the largest investor in African infrastructure, targeting key sectors such as transportation, education, health and agriculture. In summary, it is possible to note that Beijing 'generates soft power through the production of admiration, inspiration and gratitude' (Vuving, 2009).

Another important point to mention is the dual dimension of China's soft power. Unlike the general view which perceives soft power as a means of improving the international standing of a country, the Chinese leadership conceives soft power as a crucial tool for rallying popular support for the Communist Party of China, and it provides a sense of national pride (Huang, 2013, p. 7). This dimension encourages the Chinese leadership to adopt and promote soft power.

Given that China's rising hard power over the last few decades has worried the outside world, Beijing has begun to invest more heavily in soft power. As a reflection of this investment, academic interest in China's soft power has increased dramatically. However, this popularity poses some risks to researchers and policymakers. As 'soft power now seems to mean everything' (Gelb, 2009, p. 69), this concept faces the risk of losing its substance and analytical features. Besides, although its meaning has been stretched over time, it would be wrong to interpret soft power as a remedy for all cases. Soft power does not always achieve the targeted outcomes. Sometimes foreign policy objectives might be better suited to hard power practices, or the combination of both soft and hard power. Thereby, the

overreliance on soft power can negatively affect policymakers' strategic decisions, limiting their choice between different power tools. This is why a greater importance should be attached to the concept of smart power, which was developed 'to counter the misperception that soft power alone can produce effective foreign policy' (Nye, 2011, p. 20).

### Revisiting the concept of smart power

Smart power seems to be one of the latest buzzwords in the IR literature. Suzanne Nossel coined this concept in a March 2004 article in *Foreign Affairs* magazine. Analyzing the Bush administration's aggressive and unilateral acts after the September 11 attacks, she put forward a new liberal internationalist approach, highlighting the importance of soft power instruments (Nossel, 2004, p. 131). The heavy reliance of the Bush administration on hard power pushed Nossel to suggest focusing on the smart use of power to promote US interests through a stable grid of allies, institutions and norms, rather than the war on terrorism (Nossel, 2004, p. 131).

Likewise, the tarnished image of the US after the war on terrorism declared by the Bush administration led Nye to reconsider the importance of soft power and emphasize that the most effective foreign policy strategies require a mix of hard and soft power resources; what he calls 'smart power'. This concept became popular following its use by Hillary Clinton, during her testimony as Secretary of State-designate in 2009. She said 'America cannot solve the most pressing problems on our own, and the world cannot solve them without America ... We must use what has been called smart power, the full range of tools at our disposal - diplomatic, economic, military, political, legal, and cultural - picking the right tool or combination of tools for each situation' (New York Times, 2009).

As mentioned before, Nye defines smart power as 'the ability to combine hard and soft power resources into effective strategies' (Nye, 2011, p. 23). This definition is far from drawing a sufficient analytical frame to understand the real substance of smart power. Considering the broadness of this definition as an opportunity to elaborate on the academic studies on this subject, it would be useful first to redefine it to avoid any misunderstanding. Cross (2011, p. 698) redefines smart power as 'the strategic and simultaneous use of coercion and co-option'. Agreeing on this definition, I suggest adding that the use of instruments of coercion or co-option should be compatible; in other words, the practices of hard and soft power should reinforce each other. It is always possible to use hard power to obtain foreign policy goals by deterring, coercing, or intervening. Still, what is important is to use hard power in a way that it will not hinder long-term attraction. Russia's gains in terms of soft power after hosting the 2014

Winter Olympic Games in Sochi faded away after Crimea's annexation. In today's world, long-term hard power might not provide the desired outcomes, as the reactions to George W. Bush's unilateral actions after September 11 demonstrated. Being aware of this reality, many international actors invest in soft power, intending to produce gratitude, sympathy, admiration and inspiration through their foreign policy practices, and their cultural and public diplomacy. Nevertheless, without hard power capabilities to back up soft power practices, it would be difficult to ensure credibility and influence. Since neither hard nor soft power alone can produce effective foreign policy, it is crucial to use them in such a way that they will reinforce each other. For instance, China's assertive rhetoric and practices concerning the disputed islands in the South China Sea might undermine its public diplomacy efforts toward the related countries.

Combining coercion and co-optation into a smart power strategy is not always easy. In order to ensure compatibility, it is of prime importance to understand the context, choose the best instruments, combine them and convert them into appropriate power behavior. Nye (2011, pp. 208–209) remarks that a smart strategy provides the answers to five questions: What goals or outcomes are preferred?; What resources are available and in which contexts?; What are the positions and preferences of the targets of influence attempts?; Which forms of power behavior are most likely to succeed?; and What is the probability of success? Likewise, according to Wilson (2008, p. 115), smart power should be built on four essential elements: the target over which one seeks to exercise power; self-knowledge and understanding of one's own goals and capacities; the broader regional and global contexts within which the action will be conducted; and the tools to be employed, as well as how and when to deploy them, both individually and in combination.

In other words, as the famous Chinese military general Sun-Tzu underlines in his well-known book 'The Art of War', winning or losing a war does not happen by chance. It is a question of method and strategy. The first step in developing a smart power strategy is clarity in terms of one's goals and intended targets, according to which the tools of power and their usage would differ. Besides, smart power requires a good knowledge of the strengths and limitations of each instrument, which the actor will use to exercise power: what can armies, sanctions, the media, aid programs and cultural activities be expected to achieve? It is crucial to know when to use which type of power to achieve one's objectives. For example, in case of conflict, would it be more effective to use sanctions, cut-off the energy supply, military posturing, high-level visits or intensive diplomacy to obtain the desired outcomes? Before deciding, all of the negative and positive aspects of these tools, the target's capabilities and possible courses of action, the



cost of different power behaviors and the context should all be taken into account.

Power always depends on context. Therefore, each international actor should adapt its policies and strategies to the 21st century context in which domestic politics and foreign policy seem to be more interconnected, and the links between economic and security considerations are intensifying (Aggarwal & Govella, 2012; Goldstein & Mansfield, 2012; Pempel, 2012). These changes require finding ways to construct smart strategies by considering which type of power behavior is most appropriate in a given context to achieve a particular goal, before choosing the related tools of power and using them to persuade, co-opt or coerce the intended target.

As there are various possible combinations of different tools of power according to the context, it would be useful to determine some criteria for judging the 'smartness' of a foreign policy action. To this end, I propose five criteria: the ability to achieve the targeted objectives; the skill to use both hard and soft power instruments in a way that they reinforce each other; good interpretation of the existing regional and global context; time planning; and compatibility with long-term interests. For instance, in the case of a territorial dispute over a group of islands, military intervention on these islands may be the fastest way to get results, but as the legitimacy of this action would be a matter of debate, it might undermine the exercise of soft power and hinder the long-term interests of the country.

Since the instruments of power are numerous and context-specific, it would be useful to examine different types of case studies to understand better the nature of smart power. In the next section, the case of China, with a special focus on the formation of the AIIB, will be examined.

### **Chinese style of smart power: the AIIB**

Although smart power became the core principle of Obama's foreign policy, this term does not refer only to the US. China, the pre-eminent emerging global player, enjoys a wide range of resources which can be used to exercise smart power, in accordance with the objective of China's 'great rejuvenation'. Since taking over as the new leader of China in November 2012, 'Xi Jinping has set out a vision for China: the Chinese dream of resurrecting Chinese power and rejuvenating the Chinese nation' (Stanzel, 2016). In spite of the fact that the precise meaning of this vision is still a matter of debate (Kallio, 2015; Kotzé, 2016; Li, 2015; Sorensen, 2015; Wang, 2014; Xiang, 2016), internationally, it is a reflection of China's will to adopt an active foreign policy approach rather than Deng Xiaoping's strategy of 'lie low, bide your time'. The Chinese dream includes not only domestic reforms to feature national prosperity and social welfare, but also international initiatives

to enhance China's stature in world politics. The Chinese rejuvenation is deeply rooted in its history, especially its experiences of the century of humiliation – the period of intervention and imperialism by Western powers and Japan between 1839 and 1949. After suffering a humiliating decline in its national status, since the proclamation of the People's Republic of China, Chinese people have desired to return their country to its national state of glory, thereby achieving the Chinese dream (Wang, 2013). To put it another way, Beijing wishes to continue its development and reinforce its national strength without intensifying fears of a 'China threat'. This is why China needs more than ever to implement a smart power strategy in order to realize the Chinese dream of resurrecting national power, since the development of soft power alone would not be sufficient to achieve this 'dream', and the exercise of hard power alone would hinder the benign and positive image of the country.

As mentioned in the previous section, Beijing enjoys a broad variety of hard and soft power resources, which it can use to obtain its preferred outcomes in foreign policy. Nevertheless, whether or not China has the ability to use them strategically and compatibly, in other words, China's effective implementation of smart power, can only be situationally determined. It would therefore be helpful to examine China's smart power potential using the creation of the AIIB as a case study.

The AIIB is a new multilateral development bank proposed by China to finance infrastructure projects in the Asia-Pacific region. It was established in June 2015 with 57 founding members.<sup>2</sup> Thirteen new countries became members in March 2017, bringing its total membership up to 70.<sup>3</sup> Membership is open to all members of the World Bank and the Asian Development Bank, and is divided into regional (countries from Asia and Oceania) and non-regional members (Weiss, 2017, p. 7). Regional members retain 75% of the total voting power. Holding a 28% stake, China is the largest shareholder of the bank, while India is the second largest with an 8% voting share. As for the AIIB's governance structure, there are a board of governors, consisting of senior government officials from each member, an executive board, comprised of nine individuals elected by regional members and three elected by non-regional members, and a presidency. Jin Liqun, former vice-minister of China's Ministry of Finance, was elected as AIIB president in January 2016 for a five-year term.

According to the AIIB Agreement (2015), the functions of the bank are:

Article 2 (i) to promote investment in the region of public and private capital for development purposes, in particular for the development of infrastructure and other productive sectors;

Article 2 (ii) to utilize the resources at its disposal for financing such developments in the region, including those projects and programs which

will contribute most effectively to the harmonious economic growth of the region as a whole, and having special regard to the needs of less developed members in the region;

Article 2 (iii) to encourage private investment in projects, enterprises and activities contributing to economic development in the region, in particular in infrastructure and other productive sectors, and to supplement private investment when private capital is not available on reasonable terms and conditions; and

Article 2 (iv) to undertake such other activities and provide such other services as may further these functions.

As far as the capital is concerned, the AIIB's initial subscribed capital is \$100 billion, with 20% paid-in and 80% callable (Weiss, 2017, p. 12). According to estimates, the total capital of AIIB amounts to two-thirds of the capital of the Asian Development Bank and almost half of that of the World Bank (Mishra, 2016, p. 166). Besides, learning from the mistakes of the Asian Development Bank and the World Bank, the AIIB will offer loans with fewer formalities, and will help in easing the 'looming liquidity drought in infrastructure financing' (Mishra, 2016, p. 168).

Even though President Xi Jinping stated that China's motivation is mainly to meet the need for infrastructure development in Asia, and also to satisfy the wishes of all countries to deepen their co-operation (Wildau & Clover, 2015), this new bank is perceived by the US as an attempt to 'create a Sino-centric financial system to rival western dominated institutions' and undermine US supremacy in global finance (Dyer, 2015). Japan has also refrained from joining the new bank due to significant American pressure. These concerns are not entirely groundless; however, it is a fact that Asian countries truly need to develop their infrastructure. According to a report published by the Asian Development Bank in 2009, around \$8 trillion of investment would be needed during the period from 2010 to 2020 to keep Asia on track in terms of its economic development (Asian Development Bank, 2009, p. 4). Similarly, World Bank economists point out that developing countries would require annual investment of \$819 billion to prevent a decrease in economic growth compared to the previous five-year period (2010–2015) (Weiss, 2017, p. 5).

This new ambitious bank is consistent with China's growing economic stature as a rising power, and China's will to elevate its status in the global economy. In spite of the fact that economics by itself is actually hard power, Beijing's AIIB attempt connects to a smart power strategy. First of all, for many years, Chinese leaders have claimed that 'the international financial institutions have failed to recognize China's rising stature in the global economy', stressing the long delay in US approval of IMF governance reforms (the US Congress approved this reform package in the late 2015),

which include the increase of China's financial contribution and voting power in the IMF (Weiss, 2017, p. 3). By creating the AIIB, China has demonstrated that it has the capability to create alternative institutions if its demands for greater formal authority are not met. And the eagerness of Asian and European countries (even US closest allies) to join the AIIB has illustrated that China's economic carrots are attractive.

In addition, by launching the AIIB, China sent the message that it is determined to promote a multi-polar world through leading new international institutions, away from Western domination. The AIIB and the New Development Bank, officially launched in July 2015 and operated by BRICS states, were the main attempts in this search for alternative forms of multilateralism. Renard (2015, p. 4) remarks that 'until recently, China was largely perceived as a reformer of the multilateral system. With the AIIB and other initiatives such as the new BRICS Development Bank [...], China increasingly appears as a soft revisionist'. Putting it another way, Beijing has tended to use the attractiveness of money with its economic development policy in parallel with its objective to promote a multi-polar world.

Besides, despite the increase in infrastructure needs in developing countries, loans offered by multilateral development banks for infrastructure projects have declined over the past decades (Weiss, 2017, p. 4). Consequently, by contributing to the infrastructure development in the region, China aims to confirm its image as a 'responsible stakeholder' rather than a 'threat' to the global order. Given that China's hard power projection, such as the confrontation over Senkaku/Diaoyu islands, the declaration of an air defence identification zone over the disputed East China Sea, and the construction of artificial islands in the disputed South China Sea, has drawn reactions from regional countries, it has been a smart move to use its economic capability to finance infrastructure projects in the region via the AIIB. Also, as a multilateral institution, the AIIB gives China the opportunity to prevent 'the missteps in previous bilateral financing arrangements' (Ikenberry & Lim, 2017, p. 11), and hence to reinforce bilateral relations.

Additionally, this initiative is related to traditional economic hard power concerns, since it allows Beijing to convert some of its excess foreign reserves into international political capital, and to promote the renminbi as a regularly used currency for international transactions. Moreover, by allowing Beijing to develop cooperative opportunities with other countries, the AIIB may help China to digest its domestic excess capacity, which constitutes an important challenge for China's economic growth. China's petrochemical, steel, aluminum and flat glass industries are facing market saturation and overcapacity, and this industrial overcapacity has a negative influence on economic growth. The OBOR and the AIIB initiatives are expected to help China to export and/or utilize its domestic excess capacity,

since the financing of infrastructure construction could alleviate this industrial overcapacity (Moak, 2017, p. 216–217). Finally, in return for this aid, Chinese companies will obtain contracts to realize infrastructure projects. It should be noted that China's development assistance to Africa in the form of infrastructure helps China to transport African oil and gas more easily and safely to the mainland, and provides Beijing with the leverage to obtain exploration and drill rights.

In sum, combining its economic hard power and its preference for multilateralism and regional development through the AIIB, China intends to obtain economic gains, as well as to maximize its political leverage in the world, projecting a powerful but benign image.

### ***Judging the smartness of the AIIB initiative***

When adopting the five judging criteria presented in the previous section in the case of the AIIB to evaluate its effectiveness as a smart power practice, first of all, it is possible to mention that the creation of the AIIB is a part of Xi's active foreign policy in accordance with the objective to realize the Chinese dream of great national rejuvenation. Beijing's success in establishing a multilateral financial institution illustrates that it has reached a certain level and seeks to influence the structure of international trade and investment relations, as 'the real world status comes from the capability to influence international thinking and future direction' (Xiao, 2016, p. 440). It is the first time Beijing has proposed, led the negotiations for, and hosted the headquarters of this kind of international institution. This initiative marks 'China's maturation from being an institution-follower to institution-builder in global governance' (Wilson, 2017).

It is worth noting that, according to a Pew Research Center survey conducted across 38 nations, in seven of the 10 EU countries involved in the study, China is considered the leading economic power, rather than the US (Pew Research Center, 2017a). Russia, Australia and Canada also hold this view. These results illustrate that China is increasingly perceived as the world's leading economic power, hence it is making progress toward the Chinese dream of national rejuvenation, taking its rightful place in the world. Also, playing the role of a financial facilitator for the new Silk Road project, the AIIB serves China's objective to connect the major Eurasian economies through infrastructure, trade and investment, in line with its security and economic interests. For instance, since the Chinese economy is heavily dependent on energy resources transported through the Strait of Malacca, Beijing's influence in this critical trade route and good relations with the littoral states around the Indian Ocean are of prime importance for China's energy security. Its geographic positioning in the Bay of Bengal

thus makes Bangladesh an indispensable partner for China to exert more influence around the Strait of Malacca. As a result, Bangladesh's Power Distribution System Upgrade and Expansion project is exclusively funded (\$165 million) by the AIIB, and this bank also approved a \$60 million loan to address Bangladesh's gas supply deficit in March 2017 (Reuters, 2017a). The AIIB-funded Duqm Port and Railway System Preparation projects in Oman 'aim to create transport facilities in a country that could become the gateway of the Persian Gulf to the Indian Ocean section of the Maritime Road' (Gabusi, 2017, p. 33). As Giuseppe Gabusi emphasises, among the countries that receive funding from the AIIB there is 'a crucial ally (Pakistan), a strategic country in the South China Sea (Indonesia), an important source of oil (Oman) and a key partner (Myanmar)' (Gabusi, 2017, p. 33).

Secondly, the launch of the AIIB was timely, since European countries were still feeling the effects of the 2008 economic crisis, and due to its uncertain future, the US-led Trans-Pacific Partnership (TPP) was not quite as attractive as it had been, even before the US withdrawal. Beijing thus managed to persuade the US allies in the Asia-Pacific region and in Europe to join the AIIB, despite US objection. The economic and financial crisis led to a 14% reduction in investment in the EU from the pre-crisis peak of 2007 (European Parliament, 2014). Considering the pressing need for more investment, the EU Infrastructure Investment Plan (Juncker Plan), aiming to boost European investment to create jobs and growth through new and existing financial resources, was introduced in 2014. The AIIB may hence overlap with EU initiatives like the Juncker Plan. Besides, the *EU-China 2020 Strategic Agenda for Cooperation* envisages mutual cooperation in 'developing smart, upgraded and fully interconnected infrastructure systems', as well as 'to explore models of infrastructure cooperation, including project bonds, project shareholding, joint contracting and co-financing, and further coordinate the cooperation among China, the EU and its Member States' (EEAS, 2013). China's willingness to provide financing for infrastructure projects in the EU's neighborhood could be an advantage for the EU, if the right cooperation mechanisms are identified. The Chinese plan to develop railway lines connecting Piraeus Port in Greece with Western Europe via the Balkans can be considered as a good example of this win-win situation. Nevertheless, it is crucial for China and the EU to resolve the tensions over Central and Eastern Europe and the Balkans, which may hinder the win-win opportunities provided by the AIIB. For example, the 2014 memorandum of understanding between China, Serbia and Hungary for the construction of the Belgrade-Budapest railway, as part of the OBOR initiative, has created tensions with the EU, as Union procurement rules have not been respected. In fact, concerns were raised at the creation of the 16+1 format (16 Central and Eastern European countries and China) in

2012, since this format was perceived as a threat to EU unity and to the EU's overall policy on China (Zalan, 2017). Greece's block of the EU statement on China's human rights record in June 2017 has inflamed EU worries that Chinese infrastructure financing and investments will enhance Beijing's political leverage on Europe, and China and OBOR-related issues will continue to divide the Union.

In addition, President Trump's withdrawal from the TPP, which was the backbone of Obama's attempt to limit China's rise, has increased uncertainty among US allies about the reliability of the US across a range of foreign and economic matters, and has thus strengthened China's hand. After President Trump's executive order formally ending US participation in the TPP, Mexico's President Enrique Peña Nieto declared that his country hopes to bolster trade with other nations and limit its reliance on the US, signaling further rapprochement with China (Mui, 2017).

Thirdly, Beijing's focus on Asia's infrastructure need is a result of a good interpretation of the existing regional context. Creating a level of economic interdependence through its OBOR and AIIB initiatives, China can deter regional countries, especially those which have territorial disputes with China, from orienting anti-Chinese actions in the future. Hence, the participation of the Philippines, Malaysia and Vietnam, countries involved in a territorial dispute with China in the South China Sea, in the AIIB has demonstrated that the attractiveness of China's economic opportunities outweighs the concerns about China's regional leadership. In other words, the AIIB provides a useful economic carrot to deal with territorial dispute and security problems China has with its neighbors. For example, the Philippines' new President, Rodrigo Duterte, even before the election, announced that 'he is willing to back down on the South China Sea dispute with China if it can build railway systems in the Philippines within his six-year term' (Navarro, 2016).

Fourthly, the AIIB allows Beijing to use its hard and soft power in such a way that they will reinforce each other. By contributing to the infrastructure development of its neighbors and improving their living standards, China can not only promote a benign image and increase its soft power, it can also create a reliable market for more Chinese-made goods. Nevertheless, although many of China's neighbors, allies and trading partners in Asia need investment in basic infrastructure (such as electricity, access to clean water, sanitation facilities and transportation), Chinese financing and investments do not translate directly into soft power and influence in recipient countries. The significant opposition to Chinese infrastructure projects in Sri Lanka and the Maldives, claiming that China's loans create a debt trap and then Beijing 'uses the debts to either acquire the projects altogether or to acquire political leverage in that country' (Stacey, 2017), has demonstrated this reality. In other words, the misuse of economic power as a soft power tool has adversely affected China's image.

When developed countries give out loans or other forms of aid, they generally impose a cap; however, this is not the case for China, which is not a member of the Development Assistance Committee, a division of the Organization for Economic Cooperation and Development that regulates aid policy (Kawashima, 2018). If a country borrows more than it can repay, it may compulsorily hand over its authority on collateralized ports, natural assets or other infrastructure, as Sri Lanka's handover of the strategic Hambantota port shows. Should these kind of practices continue, the China-led AIIB may lose its credibility and attractiveness, proving that the exercises of 'economic hard power undercut the soft power of China's narrative' (Nye, 2018). Hence, it is of utmost importance that China builds trust with other countries, creating a true win-win situation for both sides. Otherwise, the growing distrust of China could hinder the success of the OBOR and the AIIB, and damage its soft and hard power capabilities.

Besides, if China looks not only to its own interests, but also to the interests of other countries, it would indirectly benefit its own economy and development. For instance, since the new Silk Road projects will connect the underdeveloped Western provinces of China with neighboring countries, this initiative would address the visible wealth gap between different regions of China. The effects of the new Silk Road have already become visible in Xinjiang, a major trouble spot domestically for China, as Beijing opened the first long-distance high-speed line in West China, connecting Urumqi, Xinjiang's capital, with Lanzhou, the capital of neighboring Gansu province, in 2014. This line constitutes an important part of the 3000 km long China-Pakistan Economic Corridor running from Kashgar to Gwadar.

Finally, the creation of the AIIB seems compatible with China's long-term interests. China's economic strength remains a source of concern around the world, and this concern plays a crucial role in how China is viewed. Beijing thus needs to build a new and benign image. Nonetheless, Beijing's strategy to boost its international prestige seems to have generated some negative reactions, giving birth to the concept of 'sharp power'. This concept relies on 'subversion, bullying and pressure, which combine to promote self-censorship' (Economist, 2017). Christopher Walker and Jessica Ludwig, who coined this term, argue that authoritarian governments which suppress political pluralism and free expression in order to maintain power at home are seeking to manipulate their target audiences by distorting the information that reaches them (Walker & Ludwig, 2017, p. 13). In other words, rather than persuasion and attraction, authoritarian governments use manipulation and distraction to shape global public opinion. Walker and Ludwig state that 'in the case of China ... , educational and cultural initiatives are accompanied by an authoritarian determination to monopolize ideas, suppress alternative narratives, and exploit partner institutions' (Walker & Ludwig, 2017, p. 13). In this way, Beijing



is seeking to suppress criticism of the Communist Party's policies. Nye argues that sharp power is a form of information warfare and thus a type of hard power, and it threatens soft power (Nye, 2018).

In spite of the fact that Beijing sees the term 'sharp power' as a new version of the old 'China threat' rhetoric (Xinhua, 2018), this new buzzword illustrates that there are shortcomings in the actual implementation of China's soft power strategy. It is hence crucial for China to seize the opportunity offered by the AIIB to cultivate a benign and responsible image. The Pew Research Center's 2017 survey on perceptions of China shows that views of China across Africa and Latin America are generally positive, proving how Chinese investments can contribute to improving its image. Oppositely, Europeans generally hold an unfavorable view (below 50%) of China (Pew Research Center, 2017b). Still, it is remarkable that Greece, part of China's OBOR and a destination for China's direct investment, holds the highest opinion (50%) of China in the region (Pew Research Center, 2017b). This country's veto on an EU statement about China's human rights record has showed that investments and reinforced economic relations have brought political gain to China. As a multilateral institution committed to international standards and norms, the AIIB may help Beijing to restore its image, tarnished due to the 'debt trap diplomacy', and to foster its political influence in the world.

It should be noted that 16 out of 21 infrastructure projects in Asia will be realized through joint-ventures with either the World Bank or the Asian Development Bank. This collaboration may be interpreted as a weakness, but it is actually a strategic attempt to show that the AIIB is not a rival to the existing multilateral development banks, one of the criticisms lodged against the AIIB. It will also allow the AIIB to 'build its own technical capacity, by gaining hands-on experience with development financing best practices from its peers' (Wilson, 2017).

Additionally, the AIIB will allow China to 'export its surplus volumes to generate revenue and further strengthen the overseas market share of China's state-owned enterprises' (Panda, 2017), while also providing an international platform for the globalization of Chinese companies. Thereby, in terms of (economic) hard power outcomes, this bank may help China to achieve its long-term interests, such as the promotion of China's state-owned enterprises, the internationalization of the renminbi, the consolidation of its partnership with regional countries, and the elevation of its status in the global financial system.

## Conclusion

Despite a vast amount of literature on the concepts of hard and soft power, the direct study of smart power is still lacking. Yet, as a new approach to

strategic thinking, the concept of smart power deserves more credit. Studies which focus on the deficiency of smart power in the analytical sense and the analysis of different case studies, demonstrating different combinations of the tools of soft and hard power, are indispensable in terms of making smart power a more mature IR concept.

In this article I have examined the formation of the AIIB within the context of China's smart power strategy, displaying that although China does not refrain from using its hard power to coerce its neighbors, soft power practices follow these hard moves to prevent the emergence of an anti-China coalition. In other words, China accompanies the practice of hard power with investment in soft power, in an attempt to reduce the concerns about its economic and military rise, and to promote a friendly and peaceful image. The backbone of China's smart power strategy is its economic power, which is used in a smart way to have tangible or intangible outcomes, as the creation of the AIIB demonstrates. This new bank allows Beijing to combine its economic carrots with its preference for multilateralism and regional development to attain its goals and fulfill its national interests.

Due to its ability to achieve the targeted objectives, its skill in using hard and soft power in such a way that they reinforce each other, its good interpretation of regional and global contexts, its well-timed launch, and its compatibility with China's long-term interests, the AIIB meets the five criteria presented for judging the effectiveness of an initiative within the context of China's smart power approach. Yet, the risk of debt distress because of China's excessive development-oriented loans has become a concern for borrowers, who might be worried about falling into a debt trap and losing their natural resources and/or strategic assets. The cases of Sri Lanka, the Maldives and Djibouti have enflamed criticism of China. Since these practices risk undermining China's soft power efforts (already undermined due to the alleged sharp power practices), responsible stakeholder image, and China-led multilateralism efforts, they may also hinder the China-led AIIB's credibility. Considering this risk, it is worth noting that smartness might not last forever, as the success of smart power strategy depends on both hard and soft power capabilities. Beijing should revise its strategy and focus on building trust with other countries and a true win-win situation, rather than solely securing its own interests.

## Notes

1. Influence can be defined as the power to have an effect on others' behavior.
2. *Regional members*: Australia, Azerbaijan, Bangladesh, Brunei, Cambodia, China, Georgia, India, Indonesia, Iran, Israel, Jordan, Kazakhstan, Korea, Kyrgyzstan, Laos, Maldives, Mongolia, Myanmar, Nepal, New Zealand, Oman, Pakistan, Philippines, Qatar, Russia, Saudi Arabia, Singapore, Sri Lanka, Tajikistan, Thailand, Turkey, UAE, Uzbekistan and Vietnam. *Non-*

*regional members:* Austria, Denmark, Egypt, Finland, France, Germany, Iceland, Italy, Luxembourg, Malta, Netherlands, Norway, Poland, Portugal, Sweden, Switzerland and United Kingdom.

3. Afghanistan, Armenia, Belgium, Canada, Ethiopia, Fiji, Hong Kong, Hungary, Ireland, Peru, Sudan, Timor Leste, and Venezuela.

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No potential conflict of interest was reported by the authors.

## Notes on contributor

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