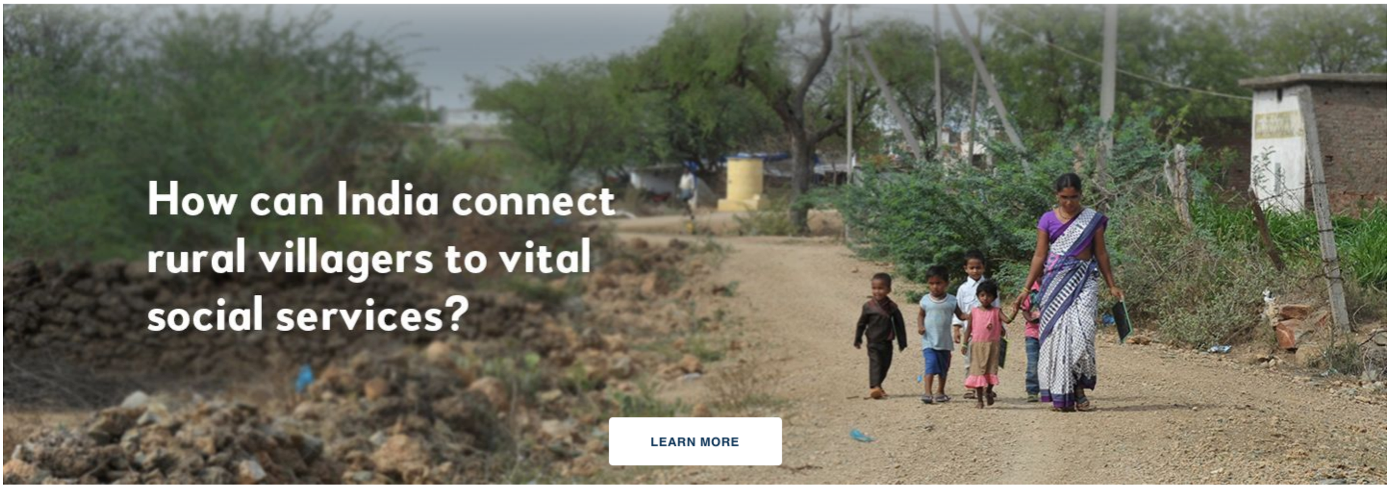
ASIAN INFRASTRUCTURE INVESTMENT BANK

HOME | OUR STRATEGIES AND PRIORITIES | OUR GOVERNANCE | HOW WE'RE DEVELOPING | HOW WE DO OUR WORK | LOOKING AND THINKING AHEAD



2018 AIIB ANNUAL REPORT AND FINANCIALS

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Our Impact

About 20 percent of Bangladesh's population doesn't have access to electricity. Poor power supply decreases the country's GDP and makes education more expensive. By investing in a combined-cycle power plant in Bhola, we're helping our client provide low-cost energy to boost the economy and uplift the lives of Bangladeshis.

Over 36 percent of the population in Madhya Pradesh, India live in poverty. Among them are tribespeople, women, children and the elderly who lack road access. We're helping India connect about 1.5 million isolated people in 5,640 villages to roads that lead to markets, schools, jobs and vital economic and social activities.

2018 at a Glance

OUR MEMBERS	OUR PROJECTS	OUR INVESTMENTS	PRIVATE CAPITAL WE'VE MOBILIZED	OUR PROFESSIONAL STAFF	OUR FEMALE PROFESSIONAL STAFF	OUR STAFF NATIONALITIES
93 69 MEMBERS 24 PROSPECTIVE MEMBERS	35	USD 7.50 BILLION	USD 715.96 MILLION	186	59 (32% OF TOTAL)	44

Messages

From Our President

The Asian Infrastructure Investment Bank (AIIB) began operations in 2016 and is now halfway through its fourth year. We are learning and growing very quickly.

Countries from across the world continue to gravitate toward AIIB, resulting in a growing membership. While this is encouraging, it raises a serious question: how can we live up to expectations? We are fully aware of the formidable challenge of meeting the diverse needs of our members and clients who are at various stages of development and from different regions. This is a difficult situation, but such challenges inspire, motivate and drive us to scale new heights and overcome difficulties. We aspire to be a development bank which responds, serves, performs and yields tangible results.

The last three years and a half have been a continuous process of institution building in many respects. A full-scale management system is taking shape. The inspiring chemistry between the Board and Management is further attuned to the needs of running the Bank and our cooperation keeps getting stronger. AIIB is charging forward with new policies being formulated and strategies being hammered out. Operational pipelines are expanding. Investment projects are being approved and executed. Disbursements are being accelerated. Monitoring, risk control and checks and balances are being implemented rigorously. The Bank's talent pool is deep and efficient. Our highly motivated staff know what AIIB's shareholders and stakeholders expect of them.

This buildup is in preparation for the challenge of infrastructure bottlenecks, the most palpable of which is the urgent demand for more effective and flexible solutions for bankable infrastructure projects in an increasingly crowded market. Some of the ways we can become a preferred provider of these financing solutions—despite our relative youth in the market—is to stress our focus on infrastructure and other productive sectors for sustainable growth by means of innovative approaches. We aim to provide new financing instruments, flexible structuring for debt and equity and long-term financing—all done at relatively low transaction costs. These are being done while maintaining risk management and high environmental, social and governance standards.

The near-term challenges are real. It is our role as a multilateral development bank (MDB) to step up during times of uncertainty to provide countercyclical lending to keep Asia on track to achieve its long-term goals. We should ramp up our efforts to attract private capital to infrastructure investments, which are usually less alluring due to a long gestation period, high uncertainty and lower rate of return.

This is why MDBs are duty-bound to push for more intense collaboration and cooperation among governments, regulators, public institutions, the private sector and all the other funding sources to make a more meaningful difference in infrastructure development under an enabling environment. For us, it means we need to be a more market- and performance-oriented financier—a facilitator to help smooth the investment process.

This is clearly a daunting task. The tall order is for us not just to satisfy Asia's need to improve connectivity through infrastructure investments. It is also to help enhance the borrower's ability to generate revenue, strengthen their debt sustainability and improve the livelihood of their people.

For many developing countries, debt financing remains an effective approach to achieving economic and social progress through critical infrastructure investment. Yet, high debt burdens can also impede the borrower's growth and development. This makes it essential for banks and borrowers in both the public and private sectors to manage debt carefully. It is incumbent upon all of us—AIIB and its members—to ensure that fiscal policies would allow for remedies when government borrowing does not align with national economic cycles.

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Cooperation with our members should not be limited to ensuring environmental and social sustainability through infrastructure. It should extend to ensuring debt sustainability as well because—in the end—the responsibility jointly falls on both lender and borrower. On both AIIB and its clients.

Such is our role, power and function in improving connectivity and cooperation. We help each other bridge the infrastructure funding gap. And as much as I'd like to stress the impact of the work we do—which this 2018 Annual Report already does succinctly—we face an inflection point for private sector investment in emerging market infrastructure.

And so, we continue to build our institution to fulfill our mission. In 2018 we made renewed efforts to shape our corporate culture. This is an aspect of building an organization that is often more complicated and comprehensive than is generally believed. Culture is fundamental to and permeates across an institution. The leadership both shapes and reflects the culture. And so I have made it an overarching priority to nurture an ethics-based corporate culture. By adhering to basic principles of professional and ethical integrity, we are building a strong foundation upon which AIIB can produce meaningful and measurable results.

As I look to the future of this 21st century bank, I am excited by the opportunity which digital infrastructure presents. Technology's potential to catalyze infrastructure investment and implementation has yet to be realized to our clients' satisfaction. Furthermore, technology upgrading is an ongoing process. It can be the link that connects our cities, our energy grids and our transport. It can unlock the potential of both rural and urban residents across the region. We will further explore how digital infrastructure can help us fulfil our mandate.

AIIB is well on its way. We are evolving our capabilities and expanding into innovative financial products. We are building a governance structure rooted in the tradition of MDBs but overlaid with a modern approach to accountability and oversight. We believe this is the right way forward for a development bank designed for the 21st century. To our members, clients, partners and staff: Thank you for accompanying us on our journey. We have only just begun.

Jin Liqun
President and Chair of the Board of Directors

From Our Board of Directors

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In 2018, the task of mobilizing infrastructure financing faced an increasingly challenging environment associated with both economic and geopolitical developments. And while AIIB is a relatively young MDB, we continue to help our members and clients prepare for uncertainties by finding innovative solutions to infrastructure financing challenges.

To prepare for these challenges, we began by evaluating how we govern ourselves, how we operate and how we aim to serve Asia and beyond. We approved a new governance model that delegates authority to the President to approve selected projects, thus enhancing efficiency and increasing the transparency of the President's accountability to shareholders. We continued to build a strong risk culture and clear reporting and performance guidelines to reinforce the Board's oversight role.

We have also strengthened our stakeholder policies—setting clear directions to ensure that concerns of project-affected people are heard and that the public's need for information are addressed. We formulated new strategies for the transport sector, private capital mobilization, investing in sustainable cities and making nonregional investments. These will further guide and focus AIIB's operations. We are committed to working with Management to develop the Bank's corporate strategy, including an effective and fit-for-purpose results monitoring framework.

In 2018, we were granted a "Permanent Observer" status by the United Nations; our triple-A ratings were reaffirmed; we were assigned a "Prime" rating based on environmental, social and governance criteria; and we aligned our approach to helping our members meet their Paris Agreement commitments. Our members totaled 93 by end-2018, and we owe it to them to sustain the achievements we attained last year.

Success entails cooperation and fostering connectivity among our members. Only together can we face the challenges to achieve the future we envisioned when AIIB was established. In our fourth year of operations we will continue to set the stage for this to happen.

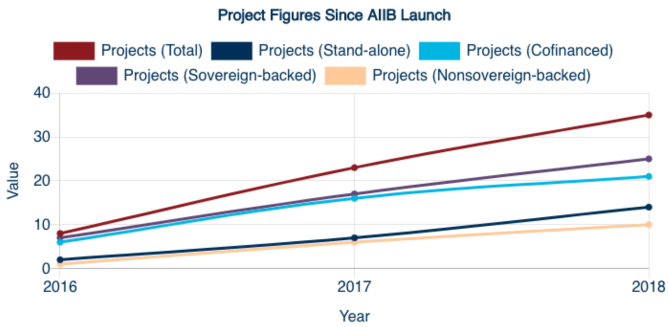
Historical Data

PROJECTS* | INVESTMENTS* | MEMBERSHIP* | STAFF* | OTHER FIGURES*

Year	Total	Stand-Alone	Cofinanced	Sovereign	Nonsovereign
End-2018	35	14	21	25	10
End-2017	23	7	16	17	6
End-2016	8	2	6	7	1

Click to generate chart

- Projects (Total)
- Projects (Stand-alone)
- Projects (Cofinanced)
- Projects (Sovereign-backed)
- Projects (Nonsovereign-backed)



Cumulative as of indicated year-end. Membership numbers aggregated (members plus prospective members).

*** For sovereign-backed stand-alone and cofinanced investment projects, in accordance with International Open Competitive Tendering (IOCT) procedures.*

2018: The Year That Was

Jan. 16

Year 2 — We celebrated our second anniversary.

Feb. 24

We released our Strategy on Financing Operations in Non-Regional Members.

April 5

We adopted our Strategy on Mobilizing Private Capital for Infrastructure.

April 11

We approved our Accountability Framework, a governance model that enhances efficiency and makes our President more responsible and accountable to shareholders.

April 18

We signed a Memorandum of Understanding with the African Development Bank and the African Development Fund to collaborate on sustainable economic development.

May 1

We approved two new prospective members (Papua New Guinea [regional] and Kenya [nonregional]), increasing our membership to 86. +2

June 25

We held our third Annual Meeting of the Board of Governors in Mumbai, India.

We launched our inaugural AIIB Yearbook of International Law ("Good Governance and Modern International Financial Institutions") based on our AIIB Legal Conference.

We signed a Memorandum of Understanding with the Islamic Development Bank Group to establish a framework for strategic cooperation and project cofinancing.

June 26

We approved Lebanon as a regional prospective member, increasing our membership to 87. +1

We held our inaugural Asian Infrastructure Forum in Mumbai, India.

July 11

AAA/F1+ — Fitch Ratings reaffirmed our AAA/F1+ rating.

July 13

S&P Global Ratings reaffirmed our AAA/A-1+ rating. AAA/A-1+

Aug. 21

Aaa/Prime1

Moody's Investors Service reaffirmed our Aaa/Prime-1 rating.

Oct. 9

We released our Transport Sector Strategy, which will guide our transportation infrastructure investments.

Oct. 11

We approved our Policy on Public Information, enhancing our transparency and accountability to the public.

Oct. 31

We signed a Memorandum of Cooperation with the Eurasian Development Bank to support project development in areas eligible for financial assistance from our respective banks.

Nov. 13

Prime C+

We received our corporate environmental, social and governance ratings from ISS-oekom (Prime C+) and Sustainalytics (66, up from 56)—a notable achievement for a young organization.

Dec. 3

We joined other MDBs in a declaration to cooperate in six key areas considered central to meeting the goals of the Paris Agreement.

Dec. 7

We approved our Sustainable Cities Strategy.

We approved our Project-affected People's Mechanism (PPM). The PPM enables project-affected people to file submissions if they believe they have been or are likely to be affected by our failure to implement our Environmental and Social Policy.

USD 7.5B

Our total approved project lending increased up to USD7.5 billion.

Dec. 19

We approved six new nonregional prospective membership applications (Algeria, Ghana, Libya, Morocco, Serbia and Togo), increasing our total membership to 93.

+6

Dec. 20

The United Nations (UN) granted us the status of Permanent Observer; we now hold a standing invitation to participate as an observer in the UN's development-focused deliberations.

2018 AIIB Annual Report and Financials

OUR STRATEGIES AND PRIORITIES

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Strategic Programming

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Our project financing decisions are based on a systematic investment planning approach. We review proposals from clients, partners and other stakeholders to achieve an appropriate balance among borrowers, sectors and sovereign/nonsovereign projects. Projects that meet the preliminary screening criteria are included in the rolling investment program which are then discussed and approved on a regular basis. This approach considers our shareholders, stakeholders, clients, financial capacity, risk-bearing capacity and staff capacity. We continue to calibrate our approach so our strategic programming matches clients' needs with our thematic priorities.

Climate Change and Green Finance

We strengthen our green investment profile through strategic programming, project preparation and monitoring. Green infrastructure accounts for the largest share of our project pipeline, expected to increase to 66 percent in the next few years.

We support our members in achieving their nationally determined contributions under the Paris Agreement and targets under the Sustainable Development Goals (SDGs). We are working with our peer MDBs to determine how we can further support our members meet these international targets and fight climate change together.

We have begun examining how innovative financing could catalyze investment in sustainable infrastructure through the announcement of the AIIB Asia ESG Enhanced Credit Managed Portfolio. AIIB can play a key role through this project to promote the integration of ESG principles in fixed-income investments in Emerging Asia.

Our Thematic Priorities

We approach investment, developing our business lines and selecting our projects based on three thematic priorities:

- Sustainable Infrastructure. We prioritize sustainable infrastructure with a focus on green investments. Along with other international financial institutions, we adopt a common approach in defining green financing. This includes investments for climate mitigation, climate adaptation and environmental protection. Green infrastructure accounts for the largest share of the Bank's approved projects, comprising around 50 percent of all projects up to 2018.

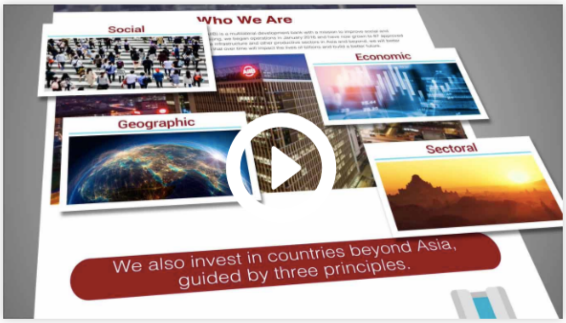
- Cross-Border Connectivity. Investing in cross-border infrastructure is one of our priorities because we believe it is key to Asia's success. Several initiatives and networks across Asia promote greater cross-border connectivity. AIIB will consider funding projects only if they follow our standards for fiscal sustainability, environmental protection and community engagement.

- Private Capital Mobilization. We seek to make investing in sustainable infrastructure in emerging markets more attractive to institutional investors. We are devising innovative solutions that pool private capital in collaboration with MDBs, governments, the private sector and other partners. Private capital has the potential to be a key part of the solution to finance Asia's infrastructure investment needs over the coming decades.

These three priorities form the foundation on which we create our sector strategies, enhance our core competencies and sharpen our focus. Client demand and stakeholder engagement validate the original rationale for our creation of these thematic priorities and will continue to guide us in the years to come.

Our New Strategies

Our strategies guide our decision-making when financing our clients' infrastructure projects. In 2018, our Board of Directors approved four such strategies.



Strategy on Financing Operations in Non-Regional Members

We prioritize investments in the region but also consider projects elsewhere if they offer significant benefits to Asia. Our Strategy on Financing Operations in Non-Regional Members proposes three principles for determining the eligibility of investments in nonregional members. Proposed projects aligned with any of these principles may be considered for financing. These principles provide that the investment should (1) support trade and connectivity with Asia, (2) promote global public goods and (3) be geographically near to and economically integrated with Asia.

Strategy on Mobilizing Private Capital for Infrastructure

The infrastructure financing gap in Asia is significant and growing. Private capital sources, specially from institutional investors, are a key part of the solution in bridging this gap. We aim to catalyze these funding sources through our Strategy on Mobilizing Private Capital for Infrastructure. The strategy further defines our approach to making investments in emerging market infrastructure more attractive to private investors. It also identifies and sequences short- and medium-term priority activities.

Transport Sector Strategy

The investment needed for transport infrastructure to support trade and economic growth in Asia is estimated at USD500 billion to USD900 billion a year. Multilaterals and bilaterals account for only around USD20 billion to USD25 billion in transport project investments per year. Our Transport Sector Strategy outlines the Bank's vision to develop sustainable and integrated transport systems that promote trade and economic growth in Asia. Priority will be placed on trunk linkages, cross-border connectivity, projects that result in transport integration and upgrading existing transport infrastructure.

Sustainable Cities Strategy

The United Nations estimates that by 2050, 1.2 billion more people will live in Asian cities. By then, Asia's urban population will account for more than 50 percent of the world's urban population. Natural resources are being strained, new cities and urban districts need to be developed and existing cities need to be retooled to improve people's quality of life. Our Sustainable Cities Strategy outlines AIIB's vision of realizing economically, environmentally and socially sustainable Asian cities that are green, resilient, efficient, accessible and thriving.

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OUR GOVERNANCE

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How We Are Governed

All the powers of AIIB are vested in our Board of Governors—our ultimate authority. The Board of Directors, elected by the Governors, is responsible for the direction of our general operations, including setting our policies and strategies and overseeing their implementation. Under the direction of the Board of Directors, the President conducts the Bank's business and is held responsible and accountable for our effective and efficient day-to-day operations.

Our Board on the Ground

To gather first-hand knowledge on how AIIB's projects impact people and businesses, members of our Board of Directors visited three AIIB member-clients in 2018. Board members gained a deeper understanding of our clients' infrastructure development challenges and relevant investment opportunities.

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In March 2018, Board members visited Indonesia where they met with the President of Indonesia, the Minister of Finance, the Minister of Public Works and housing and other officials. Some of the feedback our Board members received were that AIIB should focus on delivering projects rather than reports and studies, and that our Bank should originate and lead projects more quickly. Government officials also stressed the importance of AIIB's support for project preparation and capacity development. The delegation also visited several project sites, one of which was the AIIB-cofinanced National Slum Upgrading Project where about 9.7 million people living in 154 cities are experiencing better living conditions due to improved access to and quality of urban infrastructure.

In September 2018, Board members went to the northern part of Dhaka in Bangladesh in a visit program focused on energy. The delegation met with the State Minister of Energy and senior officials from the Ministry of Finance and were made aware of the government's ambitious energy master plan. Board delegates also visited two AIIB project sites, including a power distribution project that aims to provide about 2.5 million service connections to rural consumers and is expected to benefit about 12.5 million Bangladeshis.

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In November 2018, Board members held talks with Egypt's top officials and investment banks about the ongoing economic and regulatory framework reforms being undertaken by the government. The Prime Minister wished to see broader AIIB engagement in development projects across Egypt, especially pertaining to energy, sanitation and transportation. The delegation also visited the Benban Solar Park—a project being cofinanced by our Bank—which will provide Egypt with a clean energy alternative.

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Our Advisers

We benefit from knowledge and experience gained from an International Advisory Panel (IAP) composed of former and current high-ranking government officials as well as experts from the private sector, multilaterals and academia. The IAP supports the President and Senior Management on the Bank's strategies, policies and general operational issues. They keep us grounded by offering valuable advice and views from outside the organization.

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Three former IAP members have completed their terms: Anders Borg, Tung-Chee Hwa and Dr. Oh-Seok Hyun. In 2018, we welcomed three new advisers:

- Jose Isidro N. Camacho—Managing Director in the Asia Pacific Division of Credit Suisse based in Singapore and Vice Chair of Credit Suisse Asia Pacific. A national of the Philippines, Camacho is former Secretary of Finance and former Secretary of Energy of the Philippines.

- Dr. Myung-Ja Kim—President of the Korean Federation of Science and Technology Societies. A national of Korea, Kim is a former Minister of Environment and a former member of the National Assembly of Korea.

- Dame Meg Taylor—Secretary General to the Pacific Islands Forum. Taylor is the former Vice President and Compliance Advisor Ombudsman for the International Finance Corporation and the Multilateral Investment Guarantee Agency of the World Bank Group. Taylor is a national of Papua New Guinea.

In 2018, several IAP members took part in two events held at our headquarters, alongside the regular advisory meetings: (1) an expert roundtable dialogue on the use of sustainable investment in Asia and opportunities for collaboration and (2) a panel discussion on building an inclusive culture, as part of AIIB's internal work on building the Bank's corporate culture.

LEARN MORE [VIEW THE COMPLETE AND CURRENT LIST OF AIIB'S ADVISORY PANEL]

Accountability

After a nine-month process of in-depth engagement, in 2018 our Board approved a new model of governance in which an effective, strategic Board of Directors directs and oversees the work of an efficient, accountable management, together creating a Bank that is better able to serve clients' needs effectively and efficiently. AIIB's Accountability Framework strengthens (1) the Board's role in establishing the Bank's strategies and policies; (2) the President's role in conducting the Bank's business, such as delegating to the President the authority to approve projects except those reserved for Board consideration and (3) the Board's role in holding the President accountable for management of our Bank.

Under the framework, the President may approve certain projects based on predetermined criteria and a transparent process. The President shall submit to the Board of Directors the summaries of projects that (1) have passed Concept Review at the Investment Committee and (2) have been determined for approval within the President's authority. Changes in any project shall be submitted to the Board at the latest after the project has passed Appraisal/Final Review at the Investment Committee. We expect this governance model to make AIIB more efficient and increase our President's accountability. The framework sets clearly demarcated roles and responsibilities for the Board and Management and helps us spread a strong culture of accountability across all levels of AIIB. It lays out clear reporting and performance guidelines to reinforce the Board's oversight role. This follows best modern governance practice, appropriate for a new MDB with a nonresident Board like AIIB.

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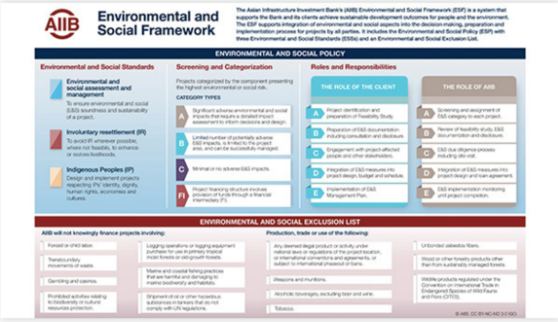
In 2018, we began establishing a strong risk culture, coupled with an Oversight Mechanism, as part of the transition to this new governance framework (which eventually came into effect Jan. 1, 2019).

Under the Accountability Framework, projects are delegated to the President for approval under specific circumstances. The framework ensures that the Board continues to have a strong voice in the project approval process by requiring projects that (1) are precedent setting, (2) have significant strategic or policy impacts or (3) meet certain dollar thresholds to go to the Board of Directors for approval. Any Board member can also request that a project which would otherwise be delegated to the President for approval be brought to the Board for its approval. The President may also undertake the decision to elevate a project to the Board for its consideration if the project presents significant reputational or integrity risks.

We believe this creates the right balance between oversight by the Board and the efficient approval of projects.



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Environmental, Social and Governance

Environmental, social and governance (ESG) agendas rank high in our corporate decision-making and organizational priorities. We are committed to promoting sustainable development by investing in infrastructure projects. These projects, in turn, are developed on the basis of our Environmental and Social Framework (ESF). Our ESF supports the Bank and its clients in achieving environmentally and socially sustainable development outcomes. It does so by integrating good international practice on environmental and social management of risks and impacts into decision-making on, and preparation and implementation of, the projects we support.

LEARN MORE [ABOUT GREEN FINANCING AT AIIB]

As AIIB expands its product offerings, we are also exploring environmental and social aspects of nontraditional projects. Managed credit portfolios and innovative efforts to attract private capital require us to explore new ways to ensure that the projects we fund improve economic outcomes and are environmentally and socially sound. To bridge this gap, we are working toward the use of an ESG approach consistent with our ESF's objectives.

A recent example is the AIIB Asia ESG Enhanced Credit Managed Portfolio, a USD500-million managed credit portfolio that aims to develop infrastructure as an asset class, develop debt capital markets for infrastructure and promote the integration of ESG principles in fixed-income investments in Emerging Asia. This project is an example of how we are promoting innovative financing mechanisms to catalyze private investments in sustainable infrastructure projects.

LEARN MORE [ABOUT THE AIIB ASIA ESG ENHANCED CREDIT MANAGED PORTFOLIO](#)

In November 2018, ESG rating agencies evaluated our Bank for the first time based on industry-specific ESG criteria.

"The Asian Infrastructure Investment Bank has established an Environmental and Social Framework (ESF), which serves to manage and minimize risks associated with the activities it finances. It includes comprehensive standards on resource efficiency, climate change and labor rights and the protection of vulnerable populations, as well as reasonable standards on pollution prevention, ecosystems and biodiversity, resettlements, community health and safety, and security personnel. AIIB forms part of the more progressive development banks, publicly disclosing individual projects financed on its website (including project overviews, financing information and project documents)."

LEARN MORE ABOUT AIIB'S ISS-OEKOM CORPORATE ESG RATING REPORT (NOVEMBER 2018)

Sustainalytics also rated AIIB for the first time, awarding a score of 66 out of 100 points. In their November 2018 ESG Rating report, the agency said that AIIB "is considered an average performer on ESG issues compared to its industry peers. AIIB's success relies on its ability to recruit and motivate a highly skilled workforce able to identify, invest in and monitor commercially sound projects with positive economic impacts. The company's ESG-related issues are overseen by the board or the executive team, suggesting that these are integrated in core business strategy."

LEARN MORE ABOUT AIIB'S ESG CREDENTIALS

Risk Governance

AIIB adheres to sound banking principles. Our risk management governance applies sound governance principles to identify, measure, monitor and control risks. It ensures that risk-taking activities are in line with our strategy and risk appetite and covers all material risk categories applicable to AIIB. To manage risk effectively, we're (1) articulating and monitoring adherence to the risk appetite, (2) leveraging a model with three lines of defense to strengthen our risk management architecture and (3) building and reinforcing the Bank's risk culture. A strong risk culture requires all staff to understand their roles and responsibilities to manage risk. To achieve this, a training and awareness campaign was launched in 2018 to help staff identify and respond to operational risks. This risk culture is being embedded throughout our organization—from the Board of Directors to the President and to Senior Management—to prepare for and manage financial, operational and other nonfinancial risks that impact our business lines. We're working on fully developing our risk management capability to support our growing business.

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Our Bank holds a strong liquidity position while conservative financial management gives us favorable financial ratios. Our financial and risk management policy design, implementation and oversight are managed by AIIB's Risk Committee, the Chief Risk Officer, the Chief Financial Officer and the Treasurer. Our risk management activities are guided by the Bank's Risk Management Framework, the Financial and Risk Management Policy and the Asset Liability Management Policy along with the directives which further define how these policies are implemented.

As the organization matures, so does its approach to risk management. In 2018, AIIB developed a more sophisticated approach to ensure the Bank can calculate its capital requirements more precisely, remain adequately capitalized in the face of adverse economic conditions and accommodate planned growth.

The Board of Directors approved the Capital Adequacy and Stress Testing (CAST) policy which (1) establishes that Economic Capital will determine the Bank's capital requirements and (2) further supports the risk culture of the Bank in line with the principles of the Risk Management Framework. This policy ensures AIIB's capital adequacy is assessed not only against the existing macroeconomic outlook, but also within the context of a severe and protracted crisis scenario.

We stress tested our business plans to determine their adherence to risk appetite based on our CAST policy approved mid-2018. The CAST policy requires stress testing of AIIB's profitability and liquidity to ensure that the Bank has robust and sound net income-generating capacity. The desired outcome of the capital adequacy test is that AIIB should have (1) sufficiently available capital to ensure it can maintain its triple-A rating even after being subjected to a severe and protracted crisis, (2) extra lending capacity to provide countercyclical lending during the same crisis period and (3) robust net income generating capacity to absorb the shock of nonperforming loans and to return to positive net income the year after reporting negative net income. To communicate all these activities and outcomes, we also strengthened our risk-related reporting.

In 2018, the Board of Directors supported our latest Risk Appetite Statement and approved the top-down allocation of risk specified therein. We define our risk capacity as the maximum level of risk the Bank can assume given its current level of resources before breaching constraints determined by available capital and liquidity needs, operational environment and obligations. The Risk Appetite Statement distinguishes between the Bank's buildup phase and its longer-term mature state, with a greater allocation made to noncore supporting activities in the buildup period. By end-2018, the Bank remained in its buildup phase.

LEARN MORE **HOW AIIB DEVELOPED ITS RISK MANAGEMENT FRAMEWORK IN PREPARATION FOR TRACKING RISK-ADJUSTED RETURN ON CAPITAL**

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Financial Governance

We use sound principles of financial management to ensure sustainable financial viability and enable us to implement our mandate effectively. We're building up our reserves and profitability to increase the Bank's operational capacity. Such a practice protects us from having to make a call on the Bank's capital that is not yet paid in and from having to resort to future shareholder capital increases. It also assures our resilience during crises while maintaining our ability to provide countercyclical financing. These ensure our financial resilience to withstand events of market stress while safeguarding our triple-A ratings as we move toward self-sufficiency in providing financing.

Financial Crime Risk Management

In September 2018, we began establishing the roles and responsibilities of the Bank's compliance function. We laid out guidelines for the assessment, monitoring and control of the risk of legal or regulatory sanctions, material financial loss or reputational loss the Bank may suffer due to failure to comply with laws, regulations, rules, related self-regulatory organization standards and codes of conduct applicable to AIIB's activities.

AIIB began initiatives to establish a fit-for-purpose Bankwide compliance function with focus on financial crime risk, particularly the anti-money laundering and combating the financing of terrorism (AML/CFT) framework. Accordingly, our AML/CFT Directive was approved and became effective by end-2018. The directive establishes the Bank's AML/CFT framework and ensures its effective implementation by laying down principles and guidance to safeguard the Bank and its personnel from being misused for money laundering, the financing of terrorism or other illicit activities. The directive serves as the cornerstone of the Bank's AML/CFT framework and reinforces AIIB's principle of zero tolerance for money laundering and financing of terrorism. To further implement the AML/CFT Directive, the Counterparty Due Diligence and Know Your Counterparty Administrative Guidance (CDD/KYC AG) was drafted and underwent consultations with internal stakeholders.

LEARN MORE **HOW AIIB PERFORMED IN TERMS OF FINANCIAL SUSTAINABILITY**

Assurance and Advisory Services

Our Bank receives professional and objective assurance and advisory services designed to add value and improve AIIB's operations. The Internal Audit Office (IAO) enhances and protects organizational value by providing risk-based and objective assurance, advice and insight. IAO helps AIIB accomplish its objectives by bringing a systematic, disciplined approach to evaluating and improving the effectiveness of governance, risk management and control processes.

In 2018, IAO led a cross-department effort under an advisory assignment on a Committee of Sponsoring Organizations of the Treadway Commission (COSO) 2013 Framework on internal control gap analysis. The analysis was completed in April 2018. By year-end, the Office of the Controller took over to close the gaps. Three mandatory training workshops were conducted to reinforce knowledge on the COSO Framework and share best practice on how to close the gaps efficiently, effectively and economically.

Who We Serve

Our Members

In 2017 and only in its second of year of operations, AIIB became the second-largest MDB in the world based on membership size. By end-2018, continued rapid membership growth to 93 signified our international relevance. Members' interest in and high expectations of the Bank make it important for us to maintain effective engagement with them as primary stakeholders.

Here is a comparative view of AIIB's membership numbers over the years:

Year	Total	Regional	Nonregional	Member-Clients
End-2018	93	50	43	13
End-2017	84	46	36	12
End-2016	57	37	20	7

Click to generate chart

- Membership (Total)
- Membership (Regional)
- Membership (Nonregional)
- Membership (Member-Clients)

Our Clients

Aside from sovereign-backed investments, our Bank can also invest in nonsovereign-backed projects in partnership with the private sector, state-owned enterprises, subnationals or public-private partnerships. Our roster of clients is getting bigger, and so is our need to manage demands, expectations and relationships. In response to this demand, our Client Relations and Programming (CRP) Office was born in November 2018. CRP's role is to ensure the continuity and progress of AIIB's business development dialogues and provide systematic and program-based engagement with member-clients. CRP will conduct country program consultations—especially in members that do not yet have AIIB projects—with an initial focus on clients in South Asia and Southeast Asia. Business development, project initiation and coverage efforts are focused on clients in Central Asia, Russia and the Middle East. CRP will then develop a follow-up mechanism in select member-clients to pursue potential projects in the pipeline. This is a new approach which we believe will allow us to develop deep client relationships and a strong project pipeline by leveraging a mobile and specialized team instead of building country offices. CRP is off to a strong start and we look forward to sharing what we learn from this new model with the larger development community.

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Public Policy Consultations

AIIB's Articles of Agreement call for the creation of two major policies of particular concern to Bank stakeholders: the Policy on Public Information (PPI) and the Project-affected People's Mechanism (PPM). In early 2018, public consultations were conducted for the draft of each of these policies—with comments received via letter, email, audio/video and face-to-face consultations with government agencies, banking sectors, business communities, project implementation agencies, civil society organizations, nongovernmental organizations, MDBs and academia. In total, 116 people commented on the PPI. For the PPM, the number of persons who participated face-to-face was 111 and there were 13 written submissions representing 31 organizations.

Public Requests for Information

On Sep. 27, 2018, our Board of Directors approved the PPI, which defines what kind of information we're required to disclose, and when. The PPI replaces an interim policy adopted at the first meeting of the Board of Directors in January 2016 and builds upon AIIB's early operational experience. The PPI also protects other legitimate interests with a series of exceptions to disclosure and adopts a principles-based approach, underpinned by a presumption of disclosure and a duty of proactive disclosure.

This principles-based approach was adopted to promote maximum transparency. It is also scalable and sustainable as AIIB grows. The PPI facilitates AIIB's role as a preferred investment partner by enabling the Bank to protect legitimate interests and to command widespread stakeholder confidence.

Since the PPI's approval, we've made it easier for the public to request for and receive information online. Quarterly reports on AIIB's implementation of the PPI are available on the Bank's website.

People Affected by Our Projects

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On Dec. 7, 2018, the Board of Directors approved the PPM, which eventually came into effect on March 31, 2019 as a policy, directive and rules of procedure. The Bank's Articles of Agreement envisaged such a complaint-handling mechanism and AIIB's Board underscored the PPM's creation when it approved AIIB's Environmental and Social Policy (ESP) in 2016.

We recognize that project-affected people can suffer when projects are not well designed or implemented. In such cases, it is critical that their problems are addressed on time and with efficiency. Accordingly, AIIB's ESP requires consultations with project-affected people and the establishment of project-level grievance redress mechanisms. When such mechanisms are not created or accessible, project-affected people can approach Bank Management, and subsequently the PPM, to address their grievances.

The PPM enables project-affected people to file submissions if they believe they have been or are likely to be adversely affected by AIIB's failure to implement the ESP. Concerns of project-affected people can be submitted to Bank Management and the PPM even before project approval.

Key features of the PPM include:

- Proactively focusing on resolving problems, especially through offering a neutral alternative dispute resolution process to independently determine whether the Bank has complied with its ESP.
- Proactively bringing lessons from the experience of other MDBs and also deriving insights from the Bank's own experience.
- Incentivizing Bank clients to create project-level grievance redress mechanisms and AIIB staff and Management to actively monitor these.
- Providing confidentiality on request for project-affected people making submissions to reduce risk of retaliation.

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HOW WE'RE DEVELOPING

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Operational Performance

Investment Portfolio

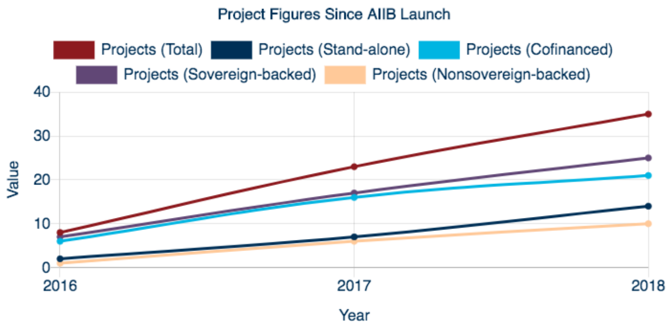
We concluded 2018 with 35 approved projects in 13 countries totaling USD7.5 billion in investments. Of the 35 projects, 31 were loan-based (USD7,050 million) and four were equity investments (USD450 million). A total of 25 projects valued at USD5,858 million (78 percent of the portfolio by value) were sovereign-backed and 10 projects valued at USD1,642 million (22 percent of the portfolio by value) were nonsovereign-backed.

Here is a comparative view of AIIB's portfolio of approved projects over the years:

Year	Total	Stand-Alone	Cofinanced	Sovereign	Nonsovereign
End-2018	35	14	21	25	10
End-2017	23	7	16	17	6
End-2016	8	2	6	7	1

Click to generate chart

- ✔ Projects (Total)
- ✔ Projects (Stand-alone)
- ✔ Projects (Cofinanced)
- ✔ Projects (Sovereign-backed)
- ✔ Projects (Nonsovereign-backed)



The energy sector continued to hold the largest share of the portfolio at 34 percent, followed by the transport sector at 24 percent, the water sector at 17 percent, finance and other productive sectors (including ICT) at 17 percent and the urban sector at eight percent.

Twenty-one projects totaling USD4,125.6 million were cofinanced operations (55 percent of approved loans and investments) while 14 projects totaling USD3,374.4 million were stand-alone operations (45 percent of approved loans and investments).

Our portfolio is expected to diversify across multiple sectors in more than 20 countries. The largest number of projects were in South Asia (15 projects). There are currently two projects that provide financing across Asia, including the IFC Emerging Asia Fund (USD150 million) and the AIIB Asia ESG Enhanced Credit Managed Portfolio (USD500 million).

Other operational milestones achieved were the implementation of the Project Prioritization and Quality Framework (PPQ), improving our operations portfolio monitoring dashboard and strengthening our project implementation and monitoring unit.

Investment Pipeline and Alignment

For the 2019-2021 pipeline, we ended the year with 64 projects totaling approximately USD9 billion. Our projects are shaped around three thematic priorities. Almost all projects in our investment pipeline were aligned with at least one of our thematic priorities (some were aligned with more than one thematic priority): three-fourths with sustainable infrastructure, a fifth with cross-border connectivity and half with private capital mobilization.

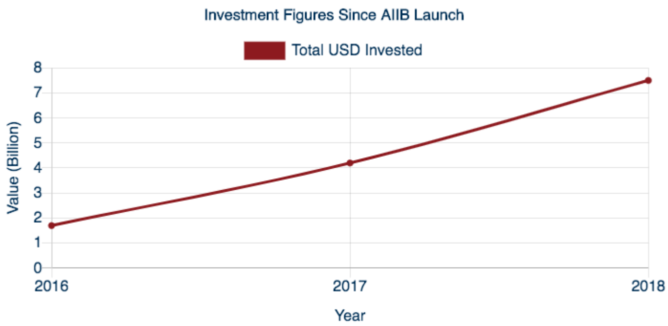
LEARN MORE **ABOUT OUR THEMATIC PRIORITIES**

Here is a comparative view of AIIB's portfolio of approved investments over the years:

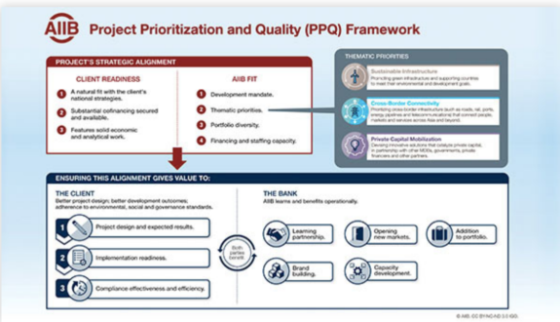
Year	Total USD Invested
End-2018	USD7.500 billion
End-2017	USD4.196 billion
End-2016	USD1.694 billion

Click to generate chart

☑ Total USD Invested



Improving Our Projects



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In 2018 we began implementing our PPQ to screen projects and ensure their strategic fit with the Bank's priorities. The PPQ allows us to focus on results and improve quality at entry and throughout the project life cycle. Five criteria built upon each other are carried through the project cycle: (1) strategic alignment, (2) value addition, (3) project design/expected results, (4) implementation readiness and (5) compliance, effectiveness and efficiency. All sovereign stand-alone projects whose preparation started from July 2018 onward were required to use the PPQ. Work on the PPQ for nonsovereign projects also began in 2018.

LEARN MORE [HOW THE PPQ IMPACTS AIIB AND THE CLIENT]

Monitoring Green Results

To measure our performance, we are further developing our results framework. Part of this is the development of guidelines on the application of shadow carbon pricing to incentivize investments in greener projects. The indicator on greenhouse gas emission reduction is a mandatory measurement for all energy projects financed by AIIB where applicable. However, it should be noted that emission reduction is only one way of measuring greenness. There are other aspects of being green (for example, environmental protection projects) that are not measured by emission reduction indicators.

Financial Sustainability

Our Shareholder Base

With the addition of two regional prospective members (Lebanon and Papua New Guinea) and seven nonregional prospective members (Algeria, Ghana, Kenya, Libya, Morocco, Serbia and Togo), our membership increased to 93 by the end of 2018, making our Bank the second largest MDB in terms of membership base. As our membership increases, so does our shareholder base, and we benefit from strong support from a broad range of shareholder members. This continued trend is testimony to our members' trust in our young Bank. We currently have USD100 billion in authorized capital, 20 percent of which has been paid in while the remaining 80 percent of capital is callable. At USD20 billion, AIIB has one of the largest paid-in capital bases of any MDB. We're committed to using our operational capital wisely, building up our reserves, planning and refining plans to avoid future capital calls.

Triple-A Reaffirmed

The triple-A short- and long-term issuer ratings given to us by Fitch Ratings, S&P Global Ratings and Moody's Investors Service in 2017 were reaffirmed in 2018. We're also operationalizing our risk policy to ensure sustainable financial viability and allow us to implement our mandate effectively, thus safeguarding our triple-A ratings.

LEARN MORE [SEE AIIB'S 2017-2019 CREDIT RATINGS REPORTS]

Return on Capital

In 2018, we continued work on implementing our Risk Management Framework and preparations for tracking the risk-adjusted return on capital (RAROC) of our investments at inception. RAROC measures the extent to which investments yield a sufficient return (hurdle rate), considering the consumption of economic capital and the cost incurred in undertaking the investments. Our RAROC calculation will continue to be dependent on cost assumptions based on peer analysis until our cost accounting system (which is still being established) is ready for implementation. This will also advance the monitoring of portfolio-level returns.

LEARN MORE [AIIB'S RISK GOVERNANCE]

Prudent Spending

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Spending patterns in 2018 show that non-human resource (HR) expenses (58 percent) were higher than HR expenses (42 percent). This is a natural profile for a new organization still in the process of developing its core operating and financial systems for Information Technology, the Risk and the Treasury functions. This higher non-HR spending trend is likely to continue for the next two years as development of these major systems is ongoing. We anticipate that the ratio of HR to non-HR costs will gradually increase starting 2020. Our Management will continue to monitor spending and manage the budget prudently.

LEARN MORE AIIB'S FINANCIAL GOVERNANCE

Financial Reporting

In 2018, a Bankwide task force on Internal Control for Financial Reporting (ICFR) established by the Office of the Controller began tracking the progress made on closing internal control gaps in areas related to financial reporting. The task force addressed these issues in gap analysis, taking us closer to ICFR compliance and strengthening our internal control. This exercise is seen to enhance the reliability of our financial statements by reducing the risk of material errors or misstatements. We will be able to refine financial reporting controls to provide reasonable assurance that the Bank's financial statements are reliable and prepared in accordance with International Financial Reporting Standards. A quarterly control report is now presented to the Board to monitor progress.

Organizational Efficiency and Capacity Building

Our Core Values

We strive to be "lean" with a small and efficient management team and highly skilled staff, making good use of human resources and talent.

We strive to be "clean" by being an ethical organization with zero tolerance for corruption.

We strive to be "green" by respecting our living planet in the course of our operations.

Our New Home

Construction of our permanent headquarters located near the Beijing Olympic Park began in September 2016 and has progressed well in 2018. Our new headquarters were designed and built with environmental sustainability features in mind. Our building progressed quickly from receiving Leadership in Energy and Environmental Design (LEED) Gold accreditation to Platinum certification. We expect to settle into our new home in 2020.

Our Human Capital

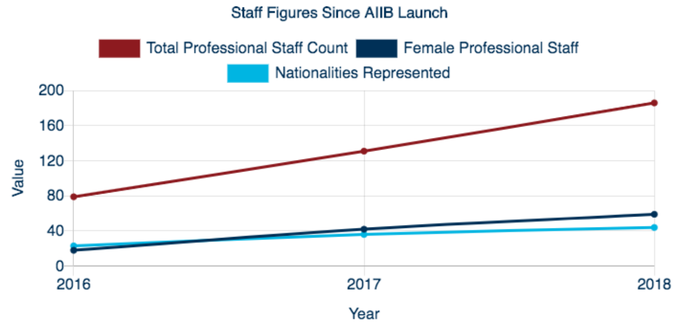
In line with our "lean" value, we remained focused on expanding when and where needed. From 2016 to 2017 our professional staff headcount increased 66 percent from 79 to 131. A year later in 2018, it increased 42 percent from 131 to 186. Our staff composition also became more diverse, increasing from 36 staff nationalities represented in the Bank in 2017 to 44 in 2018. We will continue to expand based on business needs and according to client demand, as outlined in our Strategic Programming. To support this expansion and to attract industry-leading talents, our Board of Directors approved in 2018 a revised compensation and benefits structure for Bank staff.

Here is a comparative view of AIIB's staff numbers over the years:

Year	Total Professional Staff Count	Female Professional Staff	Nationalities Represented
End-2018	186	59 (32% of total)	44
End-2017	131	42 (32% of total)	36
End-2016	79	18 (23% of total)	23

Click to generate chart

- Total Professional Staff Count
- Female Professional Staff
- Nationalities Represented



Our Staff Culture

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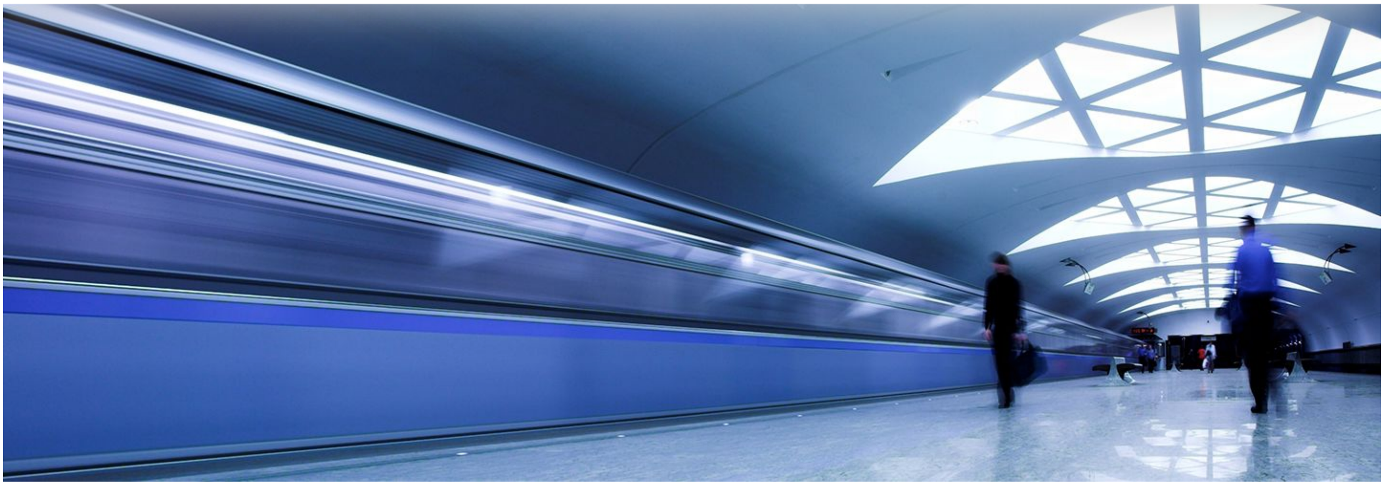
In 2018, we organized a Culture Steering Committee representing senior managers across departments. This was soon followed by the launch of our Cultural Attributes, AIIB's culture-building road map. The Human Resources Department has been working with over 70 staff volunteers to translate these attributes into concrete bottom-up programs such as idea creation, diversity and inclusion and peer-to-peer recognition. The objective is to build a unifying culture that represents AIIB's multilateralism, modernism and mission.

Our Staff Rules and Legal Framework

In 2018, the Office of the General Counsel advised and assisted the Bankwide effort to consolidate our Internal Legal Framework, enabling the interior rule of law at AIIB. The President issued critical new Staff Rules establishing ethics investigation and misconduct procedures together with implementing an Administrative Review Procedure to internally address employment-related disputes. Important new directives were also issued concerning security and safety, corporate procurement and information classification. In addition, our Staff Rules were reissued to incorporate amendments to the Policy on Compensation and Benefits agreed by the Board of Directors in September 2018.



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HOW WE DO OUR WORK

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Our Alignment With the SDGs

AIIB's establishment is critically linked to the global effort toward sustainable development and improved living standards. Understanding the Sustainable Development Goals (SDGs) is important for AIIB to effectively serve its clients. AIIB members are committed to the SDGs and many countries have integrated the goals into their road maps. For example, Bangladesh, Cambodia, China, Malaysia, Mongolia and the Philippines have all integrated the SDGs into their national development plans.

Research on the SDGs show interlinkages among the targets and sometimes interdependence between goals and targets, and that these interlinkages are critical to achieving development benefits. Mapping interlinkages between the SDGs and institutional activities is often subjective and dependent on the perception of the institution conducting the study. We consciously factored this into our own mapping exercise on two levels: (1) AIIB's activities at the institutional level in relation to the SDGs and (2) how these are aligned at the project level.

With a mandate to align the Bank's operations with global priorities, we reviewed our investment portfolio and environmental and social standards to (1) determine our alignment with the SDGs and better assess the impact of our operations and (2) see how our operations align with international agreements. We discovered that the Bank's operations are not only aligned with our investments but also with the environmental and social standards we adopt to ensure sustainable development. Moreover, the direct and indirect benefits emerging from our investments could also be aligned with specific SDGs. Broadly, our investments are focused on four major goals (SDG 6: Clean Water and Sanitation, SDG 7: Affordable and Clean Energy, SDG 9: Industry Innovation and Infrastructure and SDG 11: Sustainable Cities and Communities).

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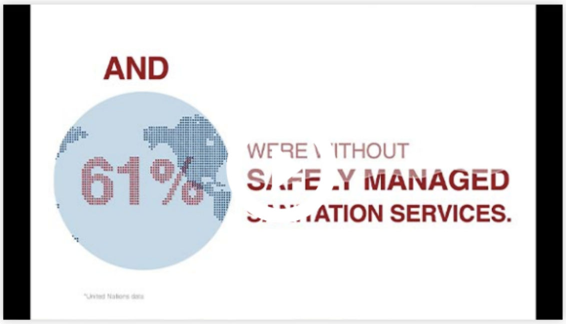
This endeavor is supplemented by the environmental and social measures aligned with SDG 8: Decent Work and Economic Growth; SDG 9: Industry, Innovation and Infrastructure; SDG 10: Reduced Inequalities; SDG 12: Responsible Consumption and Production; SDG 13: Climate Action; SDG 14: Life Below Water and SDG 15: Life on Land.

The direct and indirect benefits accrued from the investments are aligned with SDG 1: No Poverty, SDG 2: Zero Hunger, SDG 3: Good Health and Well-Being, SDG 4: Quality Education and SDG 5: Gender Equality.

As the infographic shows, the alignment of our activities is best demonstrated with case studies where specific investments, environmental and social measures and benefits can be aligned with specific SDGs.

Our activities with major global pledges for growth and development are limited to alignment mapping. Individual governments are in better positions to measure SDG impacts at the macro level, and they will have to generate relevant data for each target assigned with the SDGs.

For AIIB, it is important to decide how the Bank's investment operations align with the SDGs and how these can be depicted in project documentation.



Value for AIIB and the Client

Our Project Prioritization and Quality Framework (PPQ) helps us ensure that projects we include in our investment program are strategically aligned with the mandates of and add value to both AIIB and the client.

The PPQ allows us to ensure alignment with AIIB in terms of thematic priorities, sector priorities, portfolio diversity and the Bank's capacity. The PPQ gives us a better look at the possibility of alignment between the project and the client's national strategies, providing substantial cofinancing and solid economic and sector analytical work.

For AIIB, the PPQ allows us to look closely at what the project would bring to the Bank (for example, if it would allow us to learn, build partnerships, build our brand, open new markets or develop our capacity).

For the client, the PPQ allows us to see if (1) the project would add value to clients in terms of adding financing currently not provided by the market, (2) risks involved could be shared or mitigated, (3) the project design could be improved and (4) the project offers better development outcomes and adheres to higher ESG standards.

LEARN MORE **STRATEGIC ALIGNMENTS AND QUALITY CRITERIA INCLUDED IN THE PPQ**

Project Spotlight

EGYPT: Sustainable Rural Sanitation Services Program

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Abdel Naby Remembers Clean Waters

The scent of sewage is not a stranger to 70-year-old retiree Sayed Abdel Naby who lives near an open sewer in Sakakra village 100 kilometers northeast of Cairo, Egypt. Garbage on top of sewage increases the odor.

"We used to wash ourselves in El-Salam," Abdel Naby reminisces a time when the waters were clean. Then the water quality deteriorated. A rudimentary sanitation system—built by the villagers in 1988—drains into the canal and today causes much of the pollution.

The Sakakra sewerage is one of the polluters of the El-Salam Canal in the Nile Delta, which Egypt aims to rehabilitate as part of its National Wastewater Project. Under this umbrella project, the Sustainable Rural Sanitation Services Program was launched to strengthen institutions and policies as well as improve and increase access to sanitation services in rural Egypt. AIIB invested USD300 million for the second phase of the program, which is jointly funded by the World Bank and the Government of Egypt.

More than 7,000 Sakakra residents in the Sharkiya Delta governorate await improvements to the village's sanitation services. Residents fear the spread of disease since the polluted sewers attract mosquitoes, flies and bugs.

"The current sanitation system is outdated," says community leader Ahmed Adel. "The pipelines are too small and located just beneath the surface, causing regular flooding."

Sewage flooding into the streets creates health issues for pedestrians, says 62-year-old villager Sayed Mahmoud, adding that water from broken sewerage pipes mixes with tap water.

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Hayam, a homemaker who lives less than 100 meters from an open sewer, is concerned about the health risks poor sanitation poses to her three young children.

"The sewers are in a bad state," she says. "It's not natural and has negative effects on children and the elderly. The smell causes breathing problems and I'm worried one of my children might fall into the sewers."

College student Mohamed Helmy works in a pharmacy located next to the sewers. "Farmers use sewer water to irrigate their lands," he says. "We need a new sanitation system and the open sewers need to be closed."

Sakakra is not an exception. With an estimated 80 percent of households in rural Egypt not covered by public sewerage, improvements in the sanitation system are badly needed.

AIIB is financing both the physical infrastructure and improvement programs for institutions responsible for sanitation.

The projects will run till September 2023. In total, 178,000 households in 133 villages in the governorates of Dakahliya, Sharkiya, Damietta, Menoufya and Gharbiya will receive sanitation services.

Technical studies to determine the most suitable and highest priority locations for a new drainage system are underway. Sanitation projects in Egypt used to be conducted top-down by the government, but this one takes a more community-based approach.

Abdel Naby, Hayam, Mahmoud and their neighbors' participation will help Sakakra get a new pump station, a new network of pipelines and a new wastewater treatment plant serving five villages. And hopefully along with that, newfound safety and peace of mind.

INDIA: Andhra Pradesh Rural Roads Project

ENLARGE

Navya and Sujatha's Road to Education

Thirteen-year-old Navya Reddy can't wait to go back school. A new road crosses her village in Ayyarapali in Andhra Pradesh's Prakasam district, and she's eager to share the news with her schoolmates. The road now enables the school van to pick Navya up from home instead of her having to walk a kilometer to the main district road.

Navya's family lives in one of the 4,973 habitations expected to benefit from the Andhra Pradesh Rural Roads Project, a USD666-million initiative funded by AIIB and the Government of Andhra Pradesh.

Meanwhile, in a remote village in Komarole Mandal, 35-year-old Sujatha Sooram teaches at the government's rural child care center. The upcoming road will connect Sujatha and her village to the child care center and the government primary school, making the otherwise uneven and stony pathway to school a comfortable walk for the young students.

"It's very difficult for little children to walk on this muddy path," says Sujatha. "Rains make it worse. This much-needed road would make school more accessible to village kids."

The project aims to construct 4,824 kilometers of new all-weather roads (including seven main bridges) and upgrade 3,094 kilometers of existing roads across 13 districts, with more than 250 people per habitation (each habitation is composed of several households). Majority of the population of Andhra Pradesh (approximately 50 million), one of the largest coastal states in India, live in rural regions. Rural roads comprise 60 percent of the state's total road network. This perhaps indicates an urgent need to improve roads and connect these vastly spread habitations to better health, education and trade facilities.

The newly constructed roads have caused hope to ripple among the villagers and lessen cynicism. Women, senior citizens and those in need of health care are hoping the project would provide last-mile connectivity to social services. The project has also sparked volunteerism in some of the villagers. Braving the heat wave, farmers attend to their crops in the vast fields of the largely agrarian state of Andhra Pradesh. The rural roads project has given them a reason to hope, with some of them voluntarily contributing a small part of their lands for the road construction.

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"We sow crops like groundnut, millets, chilies and even cotton, which need great care," says Bala Venkat Reddy, a farmer in Moolapali village. "With the roads, getting to our fields every day with our bullock carts is much easier now. Transporting our harvested crops to the nearest market yard now costs us half the price, with tractors and three-wheeler auto rickshaws easily accessing our village."

Roads are lifelines to socioeconomic development. They embolden women to travel farther distances for education, trade and health. They enable people like Bala Venkat to transport and trade his crops. They empower teachers like Sujatha to educate the young. And they help Navya get to school safely.

INDONESIA: Strategic Irrigation Modernization and Urgent Rehabilitation

ENLARGE

Kendo and Suhada's Thoughts on Rice and Water

Kendo is passionate when he talks about modernizing agricultural irrigation in his village of Karangwangi in Subang Regency, West Java, Indonesia. The 55-year-old farmer says water needs to be distributed equally to all rice farms, but canals are damaged and unable to proportionally irrigate arable land especially during the dry season.

Cultivating 4.5 hectares, Kendo is one of several hundred thousand farmers who rely on the canal to irrigate paddy fields. His home is one of 887,000 farmer households expected to benefit from the USD578-million Strategic Irrigation Modernization and Urgent Rehabilitation Project being cofinanced by AIIB, the World Bank and the Government of Indonesia.

"This is very important for rice farms in Subang," says Kendo, explaining that rice grows in flooded fields and requires continuous irrigation. "I hope the project can be completed soon."

The project focuses on infrastructure management, rehabilitation and modernization of 14 national irrigation systems spread across eight river basins with a service area of around 100,000 hectares. It involves strategic modernization of the 176,000-hectare Jatiluhur Irrigation Scheme in West Java, the largest contiguous irrigation system in Indonesia.

Meanwhile, Suhada, a 40-year-old farmer from Gempol Village, says agricultural modernization is needed since sometimes he doesn't get adequate amounts of water due to irrigation scheduling. He adds that modernization would solve canal clogging due to sediment particles.

"If water is not distributed in time, crops would be affected and I won't be able to harvest on time," says Suhada.

Irrigation is pivotal in Indonesia where 30 percent of the total land (about 55 million hectares) is agricultural. Agriculture is the main source of employment for more than 33 percent of the country's labor force and contributes 14 percent to gross domestic product. Modernizing the irrigation system could distribute water equally to all farms.

ENLARGE

"Irrigation scheduling is still manual but will later use an automated system of operating irrigation gates to ensure real-time water distribution for farmers who could then directly irrigate their farms when needed," says Iman Ramdhani, head of program of project executor Balai Besar Wilayah Sungai (Citarum River basin organization).

Irrigation modernization is key to wet rice cultivation in a country that is one of the world's largest rice consumers. It allows farmers to harvest high-quality crops, explore crop diversification, decrease the cost of pumping water and minimize crop failures—ultimately leading to more stable incomes for farmers like Kendo and Suhada.

TURKEY: Tuz Gölü Gas Storage Expansion Project

ENLARGE

Light and Heat for Bayram's Family

Among the hills of Turkey's central Anatolian province of Konya, 35-year-old Bayram Kaya lives a simple life, like most farmers. His family owns a modest farm where they grow wheat, barley and sugar beets. There he lives with his wife, parents, brother and five children.

At the center of their home is a rudimentary coal-fired stove that burns round-the-clock. Here they bake bread, cook meals and brew tea. Churning out thick black smoke, the stove also provides heating for the family of 10.

Bayram's is among one in five Turkish homes which aren't connected to the natural gas grid. When winter comes, staying warm can get difficult and expensive.

"There isn't a single house here without a coal stove—we use it for everything," says Bayram. "When the nights are long and freezing, the only other option is the electric heater. And when the electricity bill arrives, it may be two, three or four times higher than you expect."

Like many countries, Turkey has to import natural gas throughout the year. Prices in the international market spike with winter demand when consumers are using more gas to heat their homes. But if Turkey were able to import gas in the summer (when prices are lower) and distribute it in winter, consumers would see a significant change in their bills.

The solution lies underground, a few kilometers from Bayram's home where efforts to transform Turkey's energy grid are underway. The Tuz Gölü Gas Storage Expansion Project is a USD2.73-billion project cofinanced by AIIB and the World Bank that aims to quadruple Turkey's natural gas storage capacity using an underground facility.

The project uses a process called solution mining. Ultrasonic scanners reveal salt deposits beneath the earth, which engineers then drill into. The resulting cavern—large enough to fit the Eiffel Tower—is filled with water from the nearby Hirfanlı Dam. Dissolved in water, the salt deposits are extracted then returned to the lake. Once the underground cavern is sealed, it can be used to store natural gas year-round. The project could expand Turkey's overall underground gas storage capacity from 3.4 billion to 10 billion cubic meters.

ENLARGE

The project supports sustainable development and brings social benefits to the community. Fresh water for agricultural irrigation could be transported from the Hirfanlı Dam after the leaching process. This enhances the feeding and breeding conditions of the flamingo population and contributes to the revival of the Salt Lake ecosystem. Planting thousands of trees would balance the project's carbon footprint. Renewable energy could be produced by a solar power plant for electricity consumption.

More importantly, the project ensures reliable and year-round gas supply and contributes to hedging winter consumption. More storage capacity means greater ability for BOTAŞ—Turkey's largest natural gas import company—to absorb market fluctuations in demand and prices. With more supply storage, natural gas can be purchased when prices are low. It also leaves room for planning when demand is high. This ultimately passes savings to the consumer.

Among these potential consumers are the 10 members of Bayram's family, where a coal-fired stove continues to burn round-the-clock at the center of their home.

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LOOKING AND THINKING AHEAD

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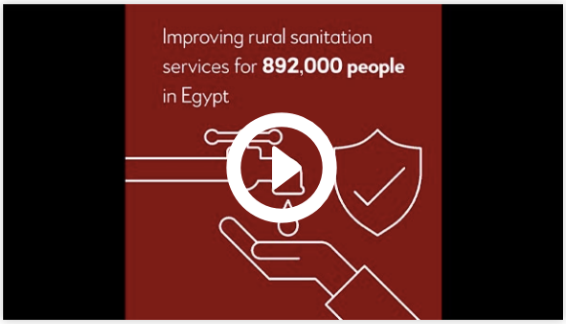
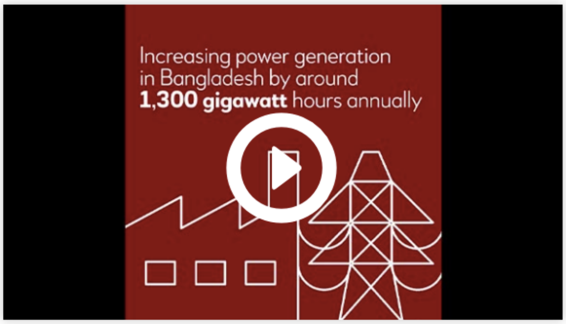
Looking and Thinking Ahead



In our third year of operations in 2018, we made significant progress in laying the core foundations of our Bank, undertaking high-quality investments and maintaining financial sustainability. We expect our start-up phase to be completed by end-2020 when our core governance frameworks, strategies, policies and infrastructure will be in place.

Learning from another year's experience, we've further refined our expectations and approaches for the next three-year planning horizon. Efforts will be focused on expanding the Bank's capacity to provide quality service and value addition to our clients in a lean manner. This will, in turn, require a continued focus on building our team of high-caliber staff and fostering a shared corporate culture. As the results of this process will likely become evident only gradually over time, we expect these focus areas to remain prominent over the next three years.

Since we began operations, we've carefully managed our budget to meet the needs of a start-up institution and our expanding work program. In our early years, with neither experiential data nor an established budget system in place, it was difficult to manage the uncertainties in budget preparation and execution. With growing experience, better data and operationalization of a budget management system, uncertainties in planning and executing the budget will be reduced. We will continue to improve overall budget management by (1) implementing the next phase of our budget management system, (2) creating a cost accounting framework to effectively and efficiently deploy resources to support our business plan and (3) aligning all these with institutional priorities and strategic directions.



With regard to our financial performance, we expect AIIB to continue having a strong financial profile with sound capital ratios. Conditions permitting and bolstered by a strong credit rating track record, we expect to have an established presence in the global capital market.

As for our investments, we foresee demand for more flexible solutions in the infrastructure financing market. We can become a preferred provider of these financing solutions—despite our relative youth—by stressing our focus on infrastructure; long tenure; relatively low cost and transaction expenses; flexible structuring for loan and debt equity; long-term financing; risk management and high environmental, social and governance standards. Local currency financing is another measure we hope to establish to lessen risks caused by exchange rate fluctuations.

Finally, we need to manage the risks we face. We're working on effective management of principal risks: credit risk of loan and guarantee, credit risk of equity investment, market risk, liquidity risk, counterparty credit risk, model risk, operational risk and compliance among others. We need to identify emerging risks to our capital, mitigate those risks early and maintain satisfactory capital levels to ensure that our triple-A ratings on a stand-alone basis are not affected.

These are all organization-building actions we need to execute, manage and coordinate simultaneously and effectively. How will we know if we're headed in the right direction? We need to measure our overall organizational performance. In 2018 we continued working on our Corporate Results Frameworks—key performance indicators and selected portfolio results indicators which aim to measure how well our core strategic business activities meet organizational priorities.

We also need to know how efficiently and effectively organizational resources (human and financial) are used, and for this we're devising a corporate scorecard, primarily to be used as an accountability tool between the Board and Management. All other existing reporting channels (quarterly progress reports on human resources, financials, business plan milestones, budget, etc.) should complement the scorecard and enable the Board to see how the Bank is performing.

As we learn, we will continue fostering the partnerships and relationships that have helped AIIB become the institution it is today. We are ramping up our outreach to multilateral, bilateral and private sector partners because only by working together can we address the infrastructure gap the world is facing.

We believe bottlenecks in infrastructure can only be effectively resolved through partnership and risk sharing. We want to encourage a dialogue between the public and private sectors so that government policies and private financiers' objectives would be more closely aligned. This will help projects—particularly public-private partnerships—to secure funding and move forward.

We intend to play a role as innovator, convener and respected partner in this sector. Over time, we intend to make markets, mobilize interest in ESG investing principles, deepen capital markets for infrastructure in Asia and be a voice for international standards in infrastructure investing.

International cooperation and multilateralism are at the core of AIIB's DNA. We are the product of the collaboration of our 57 founding shareholders who sought to address a specific need in Asia for increased investment in infrastructure. We continue to evolve thanks to the input and support of additional shareholders who have joined us since we began operations. As we enter our fourth year, we are scaling up our business, expanding our footprint and welcoming new staff—united in our mission to improve economic outcomes in Asia and beyond.