With China set to lead a new $50 billion international financial institution, the Asian Infrastructure Investment Bank (AIIB), most of the debate has centered on the United States' futile efforts to discourage other advanced economies from joining. Far too little attention has been devoted to understanding why multilateral development lending has so often failed, and what might be done to make it work better.

Multilateral development institutions have probably had their most consistent success when they serve as "knowledge" banks, helping to share experience, best practices, and technical knowledge across regions. By contrast, their greatest failures have come from funding grandiose projects that benefit the current elite, but do not properly balance environmental, social, and development priorities.

Dam construction is a leading historical example. In general, there is a tendency to overestimate the economic benefits of big infrastructure projects in countries riddled by poor governance and corruption, and to underestimate the long-run social costs of having to repay loans whether or not promised revenues materialize. Obviously, the AIIB runs this risk.

That said, there are huge infrastructure needs across developing Asia, and it is high time for China to play a greater role in international lending institutions. Moreover, the official US argument – that China should invest its money in existing institutions, such as the World Bank and the Asian Development Bank, because a Chinese-led bank would likely have governance problems – smacks of hypocrisy. Good governance? Is the US prepared to relinquish its historical prerogative to choose the World Bank president?

Likewise, the US worries that China may use the AIIB to advance China's economic and political interests. But anyone who is even vaguely familiar with the US approach to multilateral lending knows that no other country has been as adept at exploiting its power and leverage for strategic gain.

With China's growing importance in the world order, it needs to be given space to forge its own approach to global economic leadership. Frankly, a relatively small infrastructure bank seems as good a place as any to start.

Besides, China is already pouring money into the developing world, often through highly opaque channels. To the extent that the AIIB normalizes a portion of Chinese development assistance, and subjects it to scrutiny from the new bank's advanced-country members, the new bank's existence should be all for the better.

With its penchant for constant experimentation and improvement, one might even hope that China will draw lessons and apply them to all of its developing-country lending. Who knows, maybe the existing development banks will learn something.

While the world should generally welcome China's initiative, the real question is what kind of aid developing Asia needs. Anyone who has worked in developing countries understands that weak institutions and poor governance are often far bigger obstacles to growth than a lack of funds. And, however great a project looks on paper, practical implementation is often a sobering experience. Costs invariably far exceed initial estimates, and planners often woefully underestimate the skills and funding needed to ensure maintenance and repairs.

My interpretation of the World Bank's record is that its role has been most consistently positive when it helps countries with "soft" development infrastructure: technical assistance and serving as a global knowledge bank. When its main role has been to provide financial muscle, the results have been less impressive. In China itself, for example, World Bank money has not been so important quantitatively, yet the Chinese generally credit the Bank for having helpful blueprints and information.

Indeed, a strong case can be made that development aid would be more effective if it took the form of outright grants, rather than loans that ultimately need to be repaid. Headline aid numbers might seem less impressive, but long-run results would be better. Moreover, the world is awash in liquidity right now, and even where a government's own money is inadequate, it is often possible to establish public-private partnerships to build genuinely high-return projects. Competent government is a far scarcer commodity than cash.

Unfortunately, it is far from clear that the Chinese model of infrastructure development can be exported universally. China's strong central government overwhelms opposition from people displaced by new roads, bridges, and dams, and for many years ran roughshod over environmental concerns and workers' rights. The parallels to the old Soviet Union are striking.

Some developing countries in Asia work differently. In democratic India, for example, it took eight years to rebuild Mumbai's airport, because courts forced the government to respect the rights of squatters on its outskirts.

Given the legacy of problematic loans and projects funded by Western-led infrastructure banks, it is reasonable to ask whether another one is needed, as opposed to reforming existing institutions. Still, if the AIIB views itself mainly as a knowledge bank, rather than a funding vehicle, it could provide real added value. We should evaluate the AIIB by how it chooses and fosters projects, not just by how much financing it provides.